PG&E CORP (PCG)

Pipeline Safety Plan Filed, Assuming Shareholders Incur $535mm In Costs

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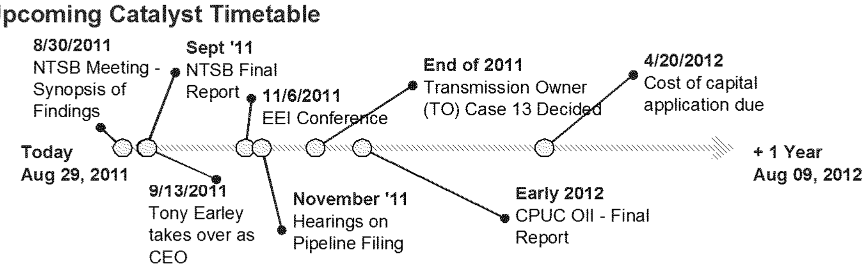
- **What Happened?:** On August 26th, PCG filed its "Pipeline Safety Enhancement Plan" with the CPUC to address pipeline pressure testing and replacement procedures, as well as retrofits to accommodate in line inspection and remote shut-off valves. The plan is in response to a June 9th request by the CPUC as part of its OIR on pipeline safety matters.
- **Financial Impact to Shareholders:** The plan would be implemented in two phases. Phase one would extend from 2011 to 2014 to coincide with the current gas rate case period, and phase II would begin in 2015. The proposal requests cost recovery for phase one only. Of the $2.2 Bn expenditure planned through 2014 ($1.4 Bn of capital, $750m of operating expense), PCG proposes that shareholders absorb a total of $535m (mostly operating expense), while the remainder is recovered in rates. The proposal calls for revenue increases of $247m, $221m and $331m in 2012, 2013 and 2014 respectively. The $535m borne by shareholders does not include ongoing costs associated with regulatory and legal proceedings and other gas pipeline-related activities outside the scope of the Pipeline Safety Enhancement Plan, nor potential fines or penalties.
- **Our Base Case Assumptions:** Our model assumes that PCG shareholders bear $1 Bn of total costs in 2011 and 2012 and that PCG's equity ratio and ROE are lowered in the 2012 cost of capital proceeding. At its current valuation, we think the stock discounts >$3 Bn of total shareholder costs. If the plan PCG filed on 8/26 is accepted the capital investments would be $0.15 accretive to our EPS forecast through 2015.
- **What's next?:** At 9:30am on Tuesday, August 30th, the NTSB will hold a public meeting to discuss its determination of the probable cause of the San Bruno disaster and to consider proposed safety recommendations. After the meeting the NTSB will release a synopsis of its findings. It will release the entire report on its website in several weeks. The CPUC procedural schedule calls for hearings on the proposal in November. PCG asks that the Commission issue a final decision by early 2012.

Upcoming Catalyst Timetable



Summary Financial Data

Ticker	**PCG**
ISI Rating	**BUY**
Price Target	**46.50**
Market Cap ($ Bn)	**16.5**
Share Price (as at 8/26/11)	**41.09**
Shares Outstanding	**400.7**
2011 Dividend Per Share	**1.82**
Dividend Yield	**4.4%**
Payout Ratio	**51.3%**

	ISI Est.		%	Consensus	
	EPS	PE	□	EPS	PE
2011E	**3.55**	11.6x	0.8%	3.52	11.7x
2012E	**3.65**	11.3x	-0.4%	3.67	11.2x
2013E	**3.50**	11.7x	-2.9%	3.60	11.4x
2014E	**3.65**	11.3x	-0.9%	3.68	11.2x

	Div Yld	+	Price Return	=	Total Return
PCG	**4.4%**	+	**13.2%**	=	**17.6%**
Group Avg	4.3%	+	2.6%	=	6.9%
Excess Total Retun					**10.6%**
Excess Return Ranking					**1 of 18**

Valuation and Risks

- Using our proprietary ISI Dividend Discount Model we value PCG at $46.50/ share, which is 13.3x our '13 consolidated EPS estimate of $3.50/ share.
- We see downside to the current stock price assuming a more significant ROE reduction in '13 and >$2000bn of incremental un-recovered San Bruno costs post 2012.
- Assuming a more benign outcome in the Cost of Capital case in '12, no more San Bruno costs we see upside to $50/share.

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PCG Financial Summary

EPS Breakdown by Division

FYE December 31,	2010A	2011E	2012E	2013E	2014E
PCG	3.45	3.58	3.70	3.50	3.68
Parent / Other	-0.02	-0.03	-0.05	0.00	-0.03
Consolidated	**3.42**	**3.55**	**3.65**	**3.50**	**3.65**

Valuation and Leverage Statistics

FYE December 31,	2010A	2011E	2012E	2013E	2014E
Price to Earnings	12.2x	11.7x	11.4x	11.9x	11.4x
EV / EBITDA	6.9x	6.2x	6.1x	6.4x	6.3x
Dividend Yield	4.4%	4.4%	4.4%	4.4%	4.4%
Return on Average Equity	12.3%	12.1%	11.9%	10.8%	10.8%
Return on Capital Employed	6.4%	7.3%	7.4%	6.8%	6.7%
LT Debt / Total Cap	46%	50%	49%	51%	51%
Total Debt / Total Cap	53%	50%	49%	51%	51%
Net Debt / EBITDA	3.0x	2.6x	2.6x	2.9x	2.9x
FFO / Total Debt	27%	28%	28%	25%	25%

Summary Consolidated Income Statement

FYE December 31,	2010A	2011E	2012E	2013E	2014E
Regulated Electric Revenue	10,644	11,466	11,808	11,857	12,114
Regulated Gas Revenue	3,196	3,211	3,211	3,211	3,211
Unregulated Generation Revenue	0	0	0	0	0
Other	1	1	0	0	0
Total Operating Revenue	**13,841**	**14,678**	**15,019**	**15,068**	**15,325**
Purchased Power / Fuel	-5,189	-5,170	-5,170	-5,170	-5,170
Gross Margin	**8,652**	**9,508**	**9,849**	**9,898**	**10,155**
Operating and Maintenance	4,432	4,782	4,939	5,037	5,136
Taxes Other Than Income	0	0	0	0	0
Other	-8,871	-9,564	-9,878	-10,073	-10,272
EBITDA	**4,213**	**4,727**	**4,910**	**4,862**	**5,019**
Depreciation and Amortization	-1,905	-1,978	-2,023	-2,063	-2,099
Operating Income	**2,308**	**2,749**	**2,887**	**2,798**	**2,920**
Interest Expense	-650	-665	-673	-731	-777
Interest and Other Income	2	149	205	226	232
Other Expense	0	-336	-500	0	0
Income from Con't Ops, Bef Tax	**1,660**	**1,897**	**1,919**	**2,293**	**2,376**
Income Tax	-547	-705	-710	-848	-879
Equity Income	0	0	0	0	0
Minority Interest	0	0	0	0	0
Preferred Stock Dividends	-14	-14	-14	-14	-14
Ajdustments / Other					
Net Income (Operating)	**1,331**	**1,422**	**1,506**	**1,437**	**1,483**
Diluted Shares Outstanding	389	401	413	411	406
Adjusted / Operating EPS	**3.42**	**3.55**	**3.65**	**3.50**	**3.65**
Dividends Per Diluted Share	1.82	1.82	1.82	1.82	1.82
Payout Ratio	53%	51%	50%	52%	50%

Summary Consolidated Statement of Cash Flow

FYE December 31,	2010A	2011E	2012E	2013E	2014E
Net Income (GAAP)	1,099	1,178	1,195	1,431	1,483
Depreciation and Amortization	2,151	2,084	2,083	2,121	2,154
Other Operating Cash Flow	-44	1,025	509	-99	-107
Cash Flow From Operations	**3,206**	**4,286**	**3,787**	**3,453**	**3,530**
Total Subsidiary Capex [1]	-3,802	-3,774	-3,882	-3,498	-3,498
Parent / Other Capex	0	-15	-20	-20	-20
Total Capital Expenditure	**-3,802**	**-3,789**	**-3,902**	**-3,518**	**-3,518**
Acquisitions	-51	0	0	0	0
Disposals	0	0	0	0	0
Other Investment Cash Flow	-4	62	0	0	0
Cash Flow From Investing	**-3,857**	**-3,727**	**-3,902**	**-3,518**	**-3,518**
Debt Issuance	862	-182	0	0	0
Securitised Debt Issuance	-404	-102	0	0	0
Subsidiary Debt Issuance	1,353	-363	516	1,302	773
Parent Debt Issuance	0	0	0	0	0
Revolver Issuance	0	103	-215	10	-20
Preferred Equity Issuance	0	0	0	0	0
Common Equity Issuance - DRIP	0	250	250	0	0
Common Equity Issuance	303	195	315	0	0
Common Equity Reductions	0	0	0	-500	0
Dividends to Common Equity	-662	-723	-751	-747	-740
Other Financing Cash Flow	-1,037	122	0	0	0
Cash Flow From Financing	**415**	**-700**	**115**	**65**	**13**
Increase / (Decrease) in Cash	**-236**	**-141**	**0**	**0**	**25**

Summary Consolidated Balance Sheet - Assets

FYE December 31,	2010A	2011E	2012E	2013E	2014E
Parent Cash and Equivalents	240	100	100	100	125
Subsidiary Cash and Equivalents	51	50	50	50	50
Accounts Receivable	944	922	922	922	922
Inventories	357	292	292	292	292
Other Current Asets	3,950	4,017	4,017	4,017	4,017
Total Current Assets	**5,542**	**5,381**	**5,381**	**5,381**	**5,406**
Total Net PP&E In Service	31,449	31,682	33,500	34,897	36,262
CWIP	0	1,563	1,650	1,743	1,841
Total Net PP&E	**31,449**	**33,245**	**35,151**	**36,641**	**38,103**
Capitalized Interest	0	31	75	121	170
Investments	0	0	0	0	0
Net Goodwill	0	0	0	0	0
Other Intangible Assets	0	0	0	0	0
Long Term Deferred Tax Assets	0	0	0	0	0
Stranded Cost Assets	0	0	0	0	0
Other Regulatory Assets	0	0	0	0	0
Other Non-Current Assets	9,034	8,916	8,916	8,916	8,916
Total Assets	**46,025**	**47,573**	**49,523**	**51,059**	**52,594**

Summary Consolidated Balance Sheet - Liabilities and Equity

FYE December 31,	2010A	2011E	2012E	2013E	2014E
Subsidiary Short Term Debt	1,662	0	0	0	0
Parent Short Term Debt	0	0	0	0	0
Short Term Securitized Debt	0	0	0	0	0
Accounts Payable	2,509	2,716	2,716	2,716	2,716
Other Current Liabilities	3,014	3,596	4,196	4,196	4,196
Total Current Liabilities	**7,185**	**6,312**	**6,912**	**6,912**	**6,912**
Subsidiary Long Term Debt	10,557	11,856	12,372	13,674	14,447
Long Term Parent Debt	349	349	349	349	349
Parent Debt (Revolver)	210	225	10	20	0
Long Term Securitized Debt	423	321	321	321	321
Long Term Deferred Tax Liabilities	5,547	5,721	5,721	5,721	5,721
Provisions	0	0	0	0	0
Other Non-Current Liabilities	10,220	10,393	10,433	10,473	10,513
Total Liabilities	**34,491**	**35,177**	**36,118**	**37,470**	**38,263**
Minority Interests	0	0	0	0	0
Preferred Equity	252	252	252	252	252
Common Equity	11,282	12,144	13,153	13,337	14,080
Total Liabilities and Equity	**46,025**	**47,573**	**49,523**	**51,059**	**52,594**

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Buy Low Risk ETR	**Buy Medium Risk ETR**	**Buy High Risk ETR**
>+10%	>+15%	>+20%
Hold Low Risk ETR	**Hold Medium Risk ETR**	**Hold High Risk ETR**
0% to +10%	-5% to +15%	-10% to +20%
Sell Low Risk ETR	**Sell Medium Risk ETR**	**Sell High Risk ETR**
<0%	<-5%	<-10%

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