

From: Cherry, Brian K
Sent: 9/19/2012 1:57:25 PM
To: Clanon, Paul (paul.clanon@cpuc.ca.gov)
Cc:
Bcc:
Subject: FW: ISI Utilities: RESEND - PCG - "Capacity to Pay" Report Released By CPSD
Appears Flawed, Target \$46.50

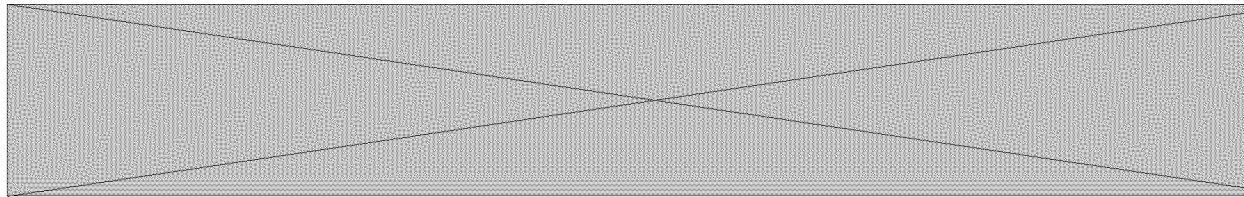
FYI

From: Togneri, Gabriel
Sent: Wednesday, September 19, 2012 1:49 PM
To: Earley Jr., Anthony; Johns, Christopher; Harvey, Kent M; Mistry, Dinyar; Pruett, Greg S.; Park, Hyun; Bottorff, Thomas E
Cc: Cherry, Brian K; Frizzell, Roger; Hayes, Kathleen (Law); Hertzog, Brian; [Redacted]
[Redacted] Bijur, Nicholas M.; Wells, Jason; Investor Relations (list)
Subject: FW: ISI Utilities: RESEND - PCG - "Capacity to Pay" Report Released By CPSD Appears Flawed, Target \$46.50

Requests/questions about the Overland Report have continued today. Greg Gordon at ISI just published the report below and like Barclays yesterday points out various ways in which the analysis by Overland is flawed.

Gabe

From: Greg Gordon [<mailto:ggordon@isigrp.com>]
Sent: Wednesday, September 19, 2012 1:34 PM
To: Investor Relations (mailbox)
Subject: ISI Utilities: RESEND - PCG - "Capacity to Pay" Report Released By CPSD
Appears Flawed, Target \$46.50



PG&E Corp (PCG)

"Capacity to Pay" Report Released By CPSD Appears Flawed; Target \$46.50

■ **What's New: CPSD Releases Consulting Report On PCG's Financing Capability.**

Yesterday (9/18/12), the Consumer Protection & Safety Division (CPSD) of the CPUC filed a substantially redacted report by an independent consultant (Overland Consulting), which opines that PCG *could* raise up to \$2.25 Bn of equity capital to pay any potential fines and or penalties associated with the San Bruno incident. The report does not attempt to address the appropriate level of fines/penalties. The report is part of testimony being prepared for all three pending San Bruno OII's.

■ **The Analysis Appears Flawed:** The Overland analysis released to the public is redacted so we have an incomplete understanding of their research. However, in our opinion, the report is simplistic and may use circular logic in arguing in part that recent underperformance of the shares means the market is implying it will willingly absorb a significant equity issuance to fund fines/penalties. This reasoning implies, by extension, that the lower the stock price falls, the higher the receptiveness of the financial market to a large dilutive financing by the company. The analysis does not appear to address many salient issues pertaining to specific and non-specific capital markets risks that could impact the ability of PCG to finance such a large quantity of equity. PCG's position is that the assessment of fines/penalties ought to be based on the facts related to the incident itself, and not solved to based on an estimate of what the company could hypothetically "afford" while still remaining financially viable.

■ **Our 2012 Equity Assumption Could Prove High, Dependent On The Level Of Fines/Penalties For San Bruno:** Our \$46.50 target price assumes total fines/penalties associated with San Bruno of \$750 million and cumulative equity issuance of ~\$1.5 billion Bn in 2012, more than twice the \$700mm amount in PCG' current financing plan (in which they have accrued for only \$200mm in penalties). Year to date they have issued \$570mm. So while the EPS *trajectory* from '13-'15 wouldn't change, if our assumption proves conservative the earnings power would rise across the forecast period accordingly. On page 2 of this note we show earnings and valuation sensitivities to different outcomes for both equity issuance and authorized ROE.

■ **PCG Still Hopes to Settle San Bruno Issues:** PCG hopes a settlement can be reached by year-end, although given the number of parties involved it may not result in all parties signing on. We believe a non-unanimous settlement, if it is supported by the CPUC Staff would be considered by the CPUC. The CPSD recently requested that the ALJ allow it to file a

consolidated fine recommendation for all three outstanding San Bruno related OII's. We expect a ruling on this issue sometime this week.

■ **Click on the link below to read the Redacted Overland Consulting report provided to CPSD Staff:**

Overland Consulting Report

If you are unable to open the link above, please copy this address and paste into your web browser:

<https://www.isihmail.com/distribution.ashx?f=v2mVdsHAXQ2WBTwzg0U13CL18Oz8pDvRXO4eVbzpGKg1&c=T3Np9iWyEp4F94tm0QLJh/>

To read the complete report, please click on the link below:

ISI Utilities: PCG - "Capacity to Pay" Report Released By CPSD Appears Flawed, Target \$46.50

If you are unable to open the link above, please copy this address and paste into your web browser:

<https://www.isihmail.com/distribution.ashx?f=x1gEVxgnc5MY1A7h7aMe6xav2B07c9fsauPSFsmvawo1&c=IvIcRw6F-Jnthf0Qxgowog2&b=4RtgNh3E6fO9xDiQ8radiA2>

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