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Sent: 10/14/2012 2:51:41 PM
To: Investor Relations (mailbox) (InvestorRelations2@pge-corp.com)
Cc:
Bcc:
Subject: PCG: Tough PD; Resolution Likely More Expensive

Equity Research

PG&E Corporation (PCG)

Tough PD; Resolution Likely More Expensive

The event: Late Friday the ALJ and Commissioner Florio issued a preliminary decision (PD) on PG&E's Pipeline Safety Implementation Plan supporting only 36% (or \$277 MM) of the requested \$767 MM revenue increase (a drag beyond the \$535 MM that PCG already accepted). PD highlights are on page 2.

Our take: We are admittedly surprised by the tough tone and big cuts in the PD coming while parties are engaged in a well-publicized settlement process; we have to assume the CPUC wanted to send a strong signal that a settlement will not come cheap. **We hope some PD terms can be modified and that this does not derail a settlement but we must assume the cost to PG&E is now moving toward \$1 BN after fines; this could slow recent PG&E enthusiasm.**

We see this as a step in the process (we hope) toward full resolution of all outstanding San Bruno issues but can see how the process could drag on given the range of stakeholder views on settling and the big financial hit to PG&E associated with the PD. A few stand out points from the PD:

- **De-rated ROE.** The order calls for PSEP related capex to earn PG&E's cost of debt (6.05% currently which we assume is pre-tax) vs an allowed after-tax ROE at 11.35% for the next 5 years; we don't like this proposal creating a residual drag on results after resolution (we want all to be done soon) and see the ROE difference creating

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a ~\$0.10 drag that will sustain through '16.

- **Pressure testing costs** of \$272 MM were denied
- **Record keeping costs** of \$228 MM were denied

Our '12-'14 EPS estimates are \$3.16, \$2.97, and \$3.34 reflecting housekeeping and are not adjusted for any additional drags with the PD.

Rating: NEUTRAL

Price (12 Oct 12, US\$): 42.50

Target price (US\$): 45.00

12/11A: 3.58

12/12E: 3.16 (from 3.23)

12/13E: 2.97 (from 3.11)

12/14E: 3.34 (from 3.47)

[Document Link \(9 Pages, 258KB\)](#)

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