



UNITED STATES

Stocks in our coverage

Regulated electric utilities:

AEP	(US\$44.19, Neutral, TP: US\$45.00)
CMS	(US\$25.28, Outperform, TP: US\$26.00)
CNP	(US\$20.24, Neutral, TP: US\$21.00)
D	(US\$53.79, Outperform, TP: US\$56.00)
DTE	(US\$62.50, Outperform, TP: US\$64.00)
DUK	(US\$67.80, Outperform, TP: US\$69.00)
EIX	(US\$46.69, Outperform, TP: US\$49.00)
HE	(US\$25.98, Neutral, TP: US\$25.00)
LNT	(US\$45.89, Outperform, TP: US\$47.00)
NU	(US\$39.91, Neutral, TP: US\$38.00)
PCG	(US\$41.51, Neutral, TP: US\$43.00)
POR	(US\$28.33, Underperform, TP: US\$25.00)
SCG	(US\$46.64, Neutral, TP: US\$47.00)
SO	(US\$44.21, Neutral, TP: US\$44.00)
TE	(US\$17.11, Neutral, TP: US\$17.00)
UIL	(US\$36.87, Outperform, TP: US\$39.00)
XEL	(US\$27.42, Neutral, TP: US\$28.00)

Diversified electric utilities:

AES	(US\$11.09, Outperform, TP: US\$12.00)
ETR	(US\$63.84, Outperform, TP: US\$69.00)
EXC	(US\$30.39, Neutral, TP: US\$32.00)
FE	(US\$39.92, Outperform, TP: US\$46.00)
NEE	(US\$72.10, Outperform, TP: US\$75.00)
PEG	(US\$30.28, Neutral, TP: US\$30.00)
PPL	(US\$29.51, Outperform, TP: US\$30.50)

Independent power producers:

CPN	(US\$19.01, Outperform, TP: US\$20.00)
DYN	(US\$20.03, Underperform, TP: US\$17.00)
NRG	(US\$23.67, Outperform, TP: US\$26.00)

Water utilities:

AWK	(US\$38.59, Outperform, TP: US\$41.00)
WTR	(US\$27.16, Neutral, TP: US\$25.50)

Note: Share prices are at close 24 January 2013.

Source: FactSet, Macquarie Capital (USA), January 2013

Analyst(s)

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25 January 2013

Macquarie Capital (USA) Inc.

US utilities and merchant power 4Q12 earnings preview

Limited (if any) margin for error

- Similar to a year ago, the winter has kicked off to a mild start in 4Q12, and weather-adjusted load growth has not recovered. Given that regulated utilities trade at an ~18% forward year PE premium vs. the S&P 500 (highest in nearly six months), earnings and buybacks expectations for IPPs continue to climb, and worries about investment grade ratings for diversified utilities continue to mount, the 4Q12 earnings season could be a nail biter. We worry that disappointing 2013 guidance issuances, reduced capex programs, and/or unfavorable hedging updates could drive sell-offs. We continue to play defense with few exceptions.
- Our top picks remain **AWK, DTE, CMS** and **EIX** for regulated utilities and **NRG, NEE** and **PPL** for IPPs/diversified utilities.

Our expectations for earnings season

- **Load growth, weather didn't help vs. guidance:** The weather was mild in 4Q12 – though HDDs were up 4% YoY nationwide HDDs were 8% below normal. We see northern utilities, especially those with gas LDCs, as being most exposed (6-9% below normal HDDs). As the weather-normalized load growth is hard to find (outside of TX and MI) with particular weakness in the MidAtlantic and the Midwest, we brace for capex delays and slower EPS growth though it's tough to say when utilities decide to reset expectations. Please see our update on load growth *CFL light bulbs must be catching on* (published this morning).
- **2013 guidance in the spotlight for some:** We expect initiations of '13 guidance for the majority of regulated and diversified utilities either during the earnings season or subsequent analyst days. We are most cautious about guidance for **POR, EXC, TE, SO** and **PEG**.

Bonus dep'n should help, while pensions a risk: Thanks to the American Taxpayer Relief Act, 50% bonus depreciation has been extended through 2013. Though this should negatively impact rate bases (watch out for those filing rate cases with forward test years in 2013 like **POR, HE, PCG, SO**), it should help cashflows and thus may (partly) bail out those with credit/equity risks in '13 (**EXC, FE, POR** and **SCG**). However pensions will likely be a YoY headwind given that the Baa yield was down 71 bps YoY as of 12/31/12. **ETR** has already indicated the higher pension expense and we expect the same for **POR** and **TE**.

- **Share buyback announcements:** The rally in shares of **NRG** and **CPN** has been partly fuelled by share buyback expectations and we expect management updates on 4Q12 earnings calls. Our estimates reflect US\$180m and US\$300m in '13 buybacks for **NRG** and **CPN**, respectively, though their free cashflows could support higher repurchases, especially for **NRG**.

Our best ideas for 4Q12 earnings season

- **Above consensus estimates:** **HE, EIX**
- **Below consensus estimates:** **TE, PEG, UIL.**

Fig 1 US utilities and merchant power: Macquarie 4Q12 earnings expectations

Company name	Ticker	Rating	Price (US\$)	Target Price (US\$)	Macquarie Consensus 4Q12	Macquarie Consensus 4Q12	% Diff.	Release date
Regulated utilities (EPS, US\$)								
American Electric Power	AEP	Neutral	44.19	45.00	0.45	0.45	-1.4%	N/A
CMS Energy	CMS	Outperform	25.28	26.00	0.24	0.24	2.6%	N/A
CenterPoint Energy	CNP	Neutral	20.24	21.00	0.24	0.21	14.3%	27-FEB-13
Dominion Resources	D	Outperform	53.79	56.00	0.68	0.69	-1.2%	31-JAN-13
DTE Energy	DTE	Outperform	62.50	64.00	0.84	0.86	-3.1%	N/A
Duke Energy	DUK	Outperform	67.80	69.00	0.63	0.64	-0.8%	13-FEB-13
Edison International	EIX	Outperform	46.69	49.00	1.07	1.04	3.2%	26-FEB-13
Hawaiian Electric Industries	HE	Neutral	25.98	25.00	0.34	0.31	8.7%	07-FEB-13
Alliant Energy	LNT	Outperform	45.89	47.00	0.58	0.57	0.5%	14-FEB-13
Northeast Utilities	NU	Neutral	39.91	38.00	0.56	0.59	-4.5%	N/A
Pacific Gas & Electric	PCG	Neutral	41.51	43.00	0.56	0.58	-4.4%	21-FEB-13
Portland General Electric	POR	Underperform	28.33	25.00	0.40	0.43	-6.2%	22-FEB-13
SCANA	SCG	Neutral	46.64	47.00	0.77	0.79	-1.5%	21-FEB-13
Southern Company	SO	Neutral	44.21	44.00	0.39	0.40	-1.3%	30-JAN-13
TECO Energy	TE	Neutral	17.11	17.00	0.16	0.21	-24.9%	05-FEB-13
UIL Holdings	UIL	Outperform	36.87	39.00	0.58	0.62	-7.0%	N/A
Xcel Energy	XEL	Neutral	27.42	28.00	0.27	0.28	-4.4%	31-JAN-13
Diversified utilities (EPS, US\$)								
AES Corp	AES	Outperform	11.09	12.00	0.29	0.29	0.5%	N/A
Entergy	ETR	Outperform	63.84	69.00	1.72	0.96	79.4%	08-FEB-13
Exelon	EXC	Neutral	30.39	32.00	0.64	0.65	-2.8%	07-FEB-13
FirstEnergy	FE	Outperform	39.92	46.00	0.82	0.83	-0.6%	26-FEB-13
NextEra Energy	NEE	Outperform	72.10	75.00	0.97	0.96	1.2%	29-JAN-13
Public Service Enterprise	PEG	Neutral	30.28	30.00	0.35	0.38	-8.9%	21-FEB-13
PPL Corporation	PPL	Outperform	29.51	30.50	0.43	0.46	-5.3%	14-FEB-13
Independent power producers (adjusted EBITDA, US\$m)								
Calpine	CPN	Outperform	19.01	20.00	317	324	-2.3%	13-FEB-13
Dynegy	DYN	Underperform	20.03	17.00	-20	-32	37.4%	NA
NRG Energy	NRG	Outperform	23.67	26.00	416	407	2.2%	NA
Water utilities (EPS, US\$)								
American Water Works	AWK	Outperform	38.59	41.00	0.30	0.40	-25.5%	27-FEB-13
Aqua America	WTR	Neutral	27.16	25.50	0.26	0.24	5.4%	NA

Source: FactSet, Macquarie Capital (USA), January 2013

Fig 2 US utilities and merchant power: changes in 4Q12 earnings estimates

	New	Old
Regulated utilities (EPS, US\$)		
AEP	0.45	0.46
CMS	0.24	0.22
CNP	0.24	0.18
DUK	0.63	0.37
EIX	1.07	1.05
HE	0.34	0.30
PCG	0.56	0.52
POR	0.40	0.39
UIL	0.58	0.59
Diversified utilities (EPS, US\$)		
AES	0.29	0.30
ETR	1.72	1.05
EXC	0.64	0.68
FE	0.82	0.92
NEE	0.97	1.00
PEG	0.35	0.33
PPL	0.43	0.44
Independent power producers (adjusted EBITDA, US\$m)		
CPN	317	321
NRG	416	394
Water utilities (EPS, US\$)		
AWK	0.30	0.35

Source: FactSet, Macquarie Capital (USA), January 2013

Fig 3 US utilities and merchant power: changes in 2012 – 2015 earnings estimates

	2012 earnings		2013 earnings		2014 earnings		2015 earnings	
	New	Old	New	Old	New	Old	New	Old
Regulated utilities (EPS, US\$)								
AEP	3.03	3.04	3.12	3.16	3.38	3.37	3.45	3.48
CMS	1.55	1.53	1.63	1.62				
CNP	1.21	1.19						
D			3.35	3.38	3.56	3.58	3.80	3.76
DUK	4.26	4.25	4.26	4.30	4.59	4.57	4.75	4.73
EIX	3.17	2.44	3.31	3.15	3.55	3.39	3.74	3.60
HE	1.62	1.59						
PCG	3.18	3.15	2.75	2.78	3.11	3.15	3.25	3.29
POR	1.90	1.88					2.08	2.07
UIL	2.04	2.05	2.29	2.35				
Diversified utilities (EPS, US\$)								
AES	1.21	1.23	1.25	1.24			1.43	1.41
ETR	6.22	5.53	4.82	5.02	4.90	5.01	5.06	5.26
EXC	2.87	2.89	2.46	2.48	2.30	2.40	2.31	2.40
FE			2.96	3.00	3.07	3.16	3.68	3.67
NEE	4.51	4.54	4.98	5.00	5.33	5.35	5.53	5.51
PEG	2.38	2.36	2.30	2.29	2.21	2.17	2.14	2.15
PPL			2.42	2.48	2.14	2.13	2.33	2.32
Independent power producers (adjusted EBITDA, US\$m)								
CPN	1,751	1,755	1,856	1,860	1,903	1,887	1,904	1,867
NRG	2,389	2,384	2,656	2,648	2,739	2,666	2,665	2,616
Water utilities (EPS, US\$)								
AWK	2.10	2.15						

Source: Macquarie Capital (USA), January 2013

Fig 4 US utilities and merchant power: changes in TPs

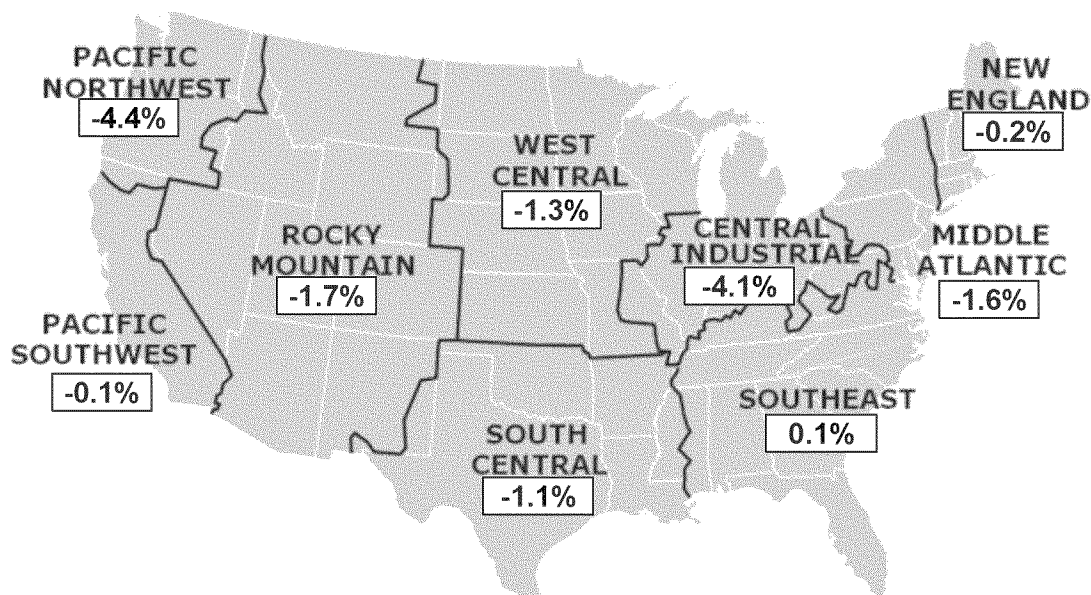
	New	Old
Regulated utilities		
CPN	US\$20	US\$19
NEE	US\$75	US\$73
PCG	US\$43	US\$44

Source: FactSet, Macquarie Capital (USA), January 2013

The changes in our 2013-2015 earnings estimates for diversified utilities and IPPs are driven by updated forward power curves, higher pension expenses and slightly lower load growth assumptions. Earnings for regulated utilities were adjusted for updated load growth and cost cutting.

Our TP for CPN increased to US\$20 (from US\$19) on the back of slightly higher estimates. Our TP for NEE increased to US\$75 (from US\$73) to reflect the company's improved regulatory visibility and potential upside to its renewable growth. We lowered our TP for PCG to US\$43 (from US\$44) due to lower earnings estimates which were driven by a higher share count and higher unrecoverable expenses.

Fig 5 YoY change in electricity demand (4Q12 vs 4Q11)



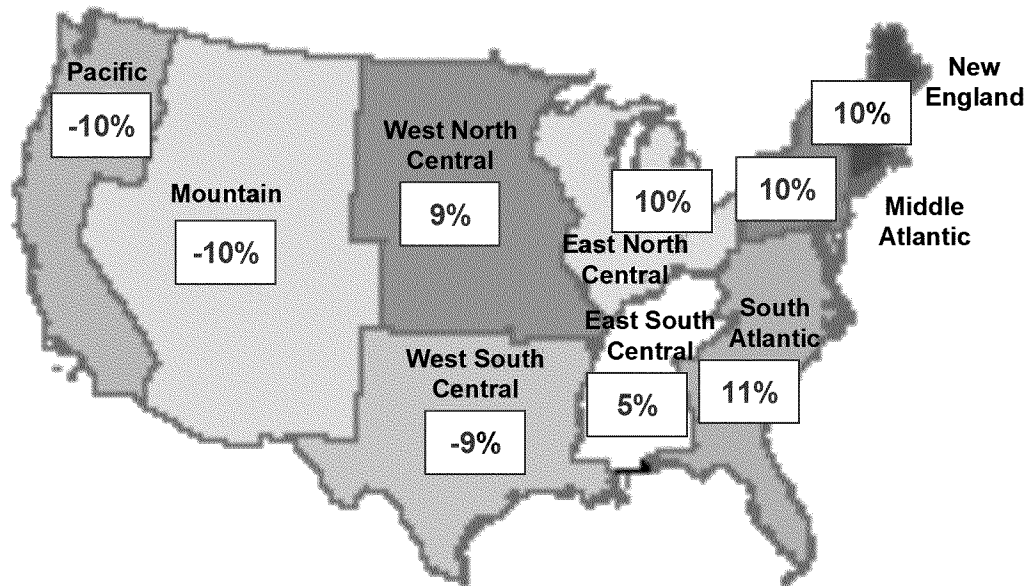
Source: EEI, Macquarie Capital (USA), January 2013

Fig 6 Power output by region (GWh)

Region	4Q12	4Q11	Change
New England	30,395	30,463	-0.2%
Mid-Atlantic	103,247	104,906	-1.6%
Central Industrial	159,821	166,577	-4.1%
West Central	77,685	78,690	-1.3%
Southeast	236,635	236,348	0.1%
South Central	148,957	150,561	-1.1%
Rocky Mountain	67,340	68,476	-1.7%
Pacific Northwest	39,761	41,612	-4.4%
Pacific Southwest	70,247	70,342	-0.1%
United States	934,088	947,974	-1.5%

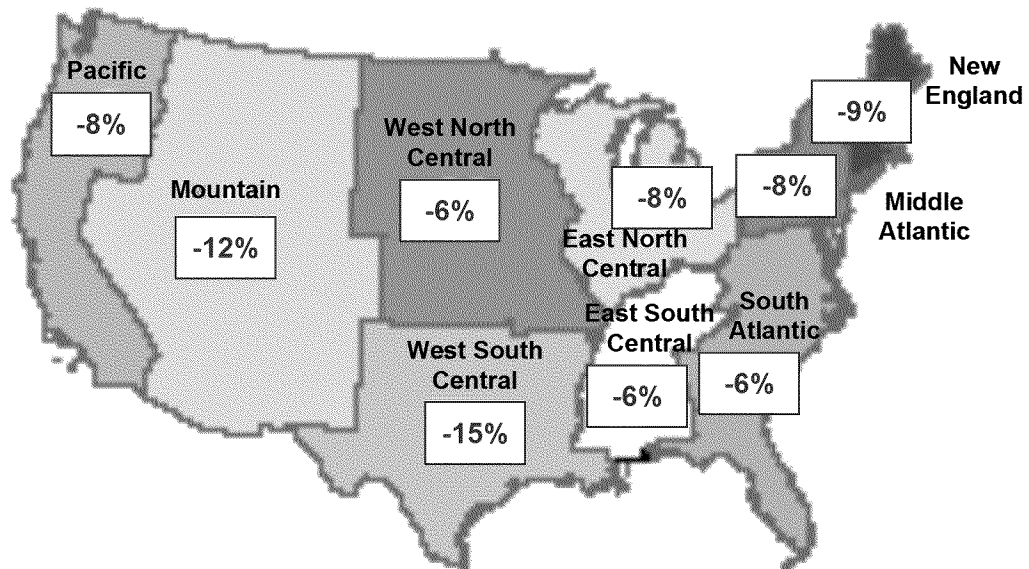
Source: EEI, Macquarie Capital (USA), January 2013

Fig 7 Changes in heating degree days (4Q12 vs 4Q11)



Source: SNL Energy, Macquarie Capital (USA), January 2013

Fig 8 Changes in heating degree days (4Q12 vs normal)



Source: SNL Energy, Macquarie Capital (USA), January 2013

Fig 9 Required disclosures – Valuation and risks

AEP	Our US\$45 TP is based on 12.9x our 2015 EPS. Risks include the outcome of court challenges to AEP's capacity pricing in OH, forward dark spreads in the Midwest in 2015 and beyond, future PJM capacity prices, the pace of economic growth and the level of market interest rates.
AES	Our US\$12 TP is based on 8.5x our '15 EPS of US\$1.41. Risks include natural gas prices in the US, the pending generation rate case in OH, the pace of economic growth, especially in Brazil and the US, monetization of non-core assets, foreign exchange and taxation on repatriated dividends.
AWK	Our US\$41 TP is based on 16.3x our 2015 EPS. Risks include: outcomes of pending and future rate cases, cost controls, and interest rates.
CMS	Our US\$26 TP is based on a PE valuation of 2015 EPS. Risks include flat or declining electric/gas delivery volumes; changes to the 2008 legislation, lower future allowed ROEs, an inability to earn the allowed ROEs, and general market risk appetite/the level of interest rates.
CNP	Our US\$21 price target is based on a sum-of-the-parts valuation on 2015E earnings, plus a scenario analysis of how the company July deploy cash. Risks include: deployment of cash (including potential M&A), commodity price exposure and win rates for field services business.
CPN	Our US\$20TP is based on 9x our '15 and normalized EBITDA. Risks include weaker forward spark spreads in ERCOT and PJM, lower than projected generation volumes, higher operating costs and/or maintenance capex.
D	Our US\$56 price target is based on 14.9x our '15 EPS and our '15 sum-of-the-parts analysis. Risks include its regulated utility capex execution in VA, biennial realized ROE review in 2013, the pace of economic growth in VA, success in winning gas infrastructure projects, forward power prices.
DTE	Our US\$64 price target is based on our 2015 sum of the parts PE valuation. Risks include lower future allowed ROEs, negative changes to the 2008 energy legislation and execution risk at the non-utility businesses.
DUK	Our US\$69 TP is based on a 14.6x our '15 EPS. Risks include the outcome of pending and upcoming rate cases in the Carolinas, the ability to retain some of the cost cutting results, regulatory response in FL to a likely shutdown of CR3, the pace of load growth in the Carolinas, OH and FL, and market interest rates.
DYN	Our US\$17 TP for DYN is based on 9x our '15 EBITDA of US\$312m, net debt of US\$973m and a 106m share count (reflecting management stock compensation). Risks include higher forward dark and spark spreads, higher pricing of new tolling agreements, and higher cost efficiencies.
EIX	Our US\$49 price target is based on 13.5x our '15 regulated utility (SCE) less parent EPS. Risks include the regulatory response to San Onofre's prolonged nuclear power outage, capex execution and the level of market interest rates.
ETR	Our US\$69 TP is based on 13x our '15 EPS and our '15 sum-of-the-parts valuation. Risks include: forward spark spreads in the Northeast, extension of nuclear operating licenses, outcomes of utility rate cases, utility load growth, as well as the future of ETR's pending transmission spin-off.
EXC	Our US\$32 TP is based on 13x our '14 EPS and our '15 sum-of-the-parts valuation. Risks include future dividend cuts, forward natural gas and power prices, forward retail volumes and margins, utility capex execution, and BGE's rate case.
FE	Our new TP of US\$46 is based on 12.5x our '15 EPS and our '15 -based sum-of-the-parts valuation. Risks include forward dark spreads in the Midwest, volumes and margins for competitive retail sales and the outcome of the pending rate case in NJ
HE	Our US\$25 target price is based on a sum of the parts on 2015E earnings. Key risks include the pace of economic growth in HI, results of the multiple rate cases for each of the three utilities in a historically tough regulatory environment, and interest rates and the impact on bank earnings.
LNT	Our US\$47 target price is based on a sum-of-the-parts PE valuation of 2015E earnings. Key risks are unfavorable rate case outcomes, economic sluggishness, investment execution and recovery.
NEE	Our US\$75 TP is based on a combination of 2014 PER and sum-of-the-parts. Risks include: the outcome of a pending rate case in FL, lower natural gas prices and further economic slowdown in Florida.
NRG	Our TP US\$26 is based on pro-forma '15 and normalized EBITDA estimated for NRG-GEN given their pending merger. Risks include regulatory approvals, merger synergies, downside to off-peak power prices and generation volumes in TX and lower retail margins and/or volumes.
NU	Our US\$38 target price is based on a sum-of-the-parts valuation of 2015E earnings. Key risks include realized synergies from the NSTAR merger, delay or cancellations in transmission investments, and economic weakness hurting sales.
PCG	We base our US\$43 price target on a 13x our 2015 EPS. Risks include recovery of spending related to the San Bruno pipeline accident; penalties associated with the accident, future equity needs, the outcome of PCG's pending general rate case, and the level of market interest rates.
PEG	Our US\$30 price target is based on 13.75x of 2014 PER and sum-of-the-parts valuation methodologies. Risks include lower forward power prices, lower than expected PJM capacity prices, utility capex execution, and slower economic recovery in NJ.
POR	Our US\$25 target price is based on a PE valuation of 2015E EPS. Risks include the results of competitive RFPs for new generation capex and the timing of such spending, regulatory uncertainty, volatility from the PCAM and the pace of economic growth.
PPL	Our US\$30.50 TP is based on 13.5x '15 EPS and our '15 sum-of-the-parts. Risks include the outcome of the pending rate case in PA, future rates for UK utilities, the pace of load growth in KY and PA, forward dark spreads and capacity prices in PJM, foreign exchange exposure
SCG	Our US\$47 target price is derived from a PE valuation of 2015E EPS. Risks include: weak economic growth in the region, the pace of nuclear capex, the outcome of potential rate cases and the levels of interest rates and inflation.
SO	Our target price of US\$44 is derived from a 14.4x PER on our 2015 EPS. Risks include: changes in regulatory environment including potentially lower allowed ROEs especially in Georgia given its upcoming rate case in the state, changes in market interest rates, slower growth in power demand and delays/cost overruns of nuclear capex.
TE	Our US\$17 price target is based on a sum-of-the-parts methodology on 2015E earnings. Risks include volumes, pricing and cost controls at TE Coal and the pace of growth in the Florida economy.
UIL	Our target price of US\$39 is based on a PE valuation of 2015E EPS. Risks include a potential rate case in CT, financing for the capital program, including equity issuance and extension of decoupling in CT.
WTR	Our US\$25.50 TP is based on 17.7x our 2015 EPS. Risks include: outcomes of pending and future rate cases, cost controls, and market interest rates.
XEL	Our TP of US\$28 is based on 13.6x (our anchor utility multiple) '15 EPS. Risks include the outcome of current and upcoming rate cases, the pace of load growth, and the level of market interest rates

Source: FactSet, Macquarie Capital (USA), January 2013

Important disclosures:

Recommendation definitions

Macquarie - Australia/New Zealand

Outperform – return >3% in excess of benchmark return
Neutral – return within 3% of benchmark return
Underperform – return >3% below benchmark return

Benchmark return is determined by long term nominal GDP growth plus 12 month forward market dividend yield

Macquarie – Asia/Europe

Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie First South - South Africa

Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Canada

Outperform – return >5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

Macquarie - USA

Outperform (Buy) – return >5% in excess of Russell 3000 index return
Neutral (Hold) – return within 5% of Russell 3000 index return
Underperform (Sell) – return >5% below Russell 3000 index return

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.

* Applicable to Australian/NZ/Canada stocks only

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:

Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*

ROA = adjusted ebit / average total assets

ROA Banks/Insurance = adjusted net profit / average total assets

ROE = adjusted net profit / average shareholders funds

Gross cashflow = adjusted net profit + depreciation

*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 31 December 2012

	AU/NZ	Asia	RSA	USA	CA	EUR	
Outperform	47.87%	54.89%	54.41%	41.93%	60.86%	44.14%	(for US coverage by MCUSA, 6.10% of stocks followed are investment banking clients)
Neutral	37.94%	26.41%	38.24%	52.16%	33.70%	27.73%	(for US coverage by MCUSA, 4.91% of stocks followed are investment banking clients)
Underperform	14.19%	18.70%	7.35%	5.91%	5.44%	28.13%	(for US coverage by MCUSA, 3.33% of stocks followed are investment banking clients)

Company Specific Disclosures:

Important disclosure information regarding the subject companies covered in this report is available at www.macquarie.com/disclosures.

Analyst Certification:

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