

Xcel Energy

Near-Term Slower Growth, Increased Capex Drive Us to the Sidelines - Downgrading to UW

▼ Underweight

Previous: Neutral

XEL, XEL US

Price: \$27.70

▼ Price Target: \$27.00

Previous: \$33.00

Xcel has seen two key growth driver changes in 2013: 1) a challenging MN rate case outcome will now likely pressure earnings growth and 2) incremental company-owned generation projects are now more likely to be built. We therefore see more of a slower growth, higher capital deployment scenario in the near term versus management's previous expectations. XEL's mild underperformance so far this year only partially reflects the MN proceedings and is bolstered in part by the potential for outer-year new generation-driven EPS growth, in our opinion. We do not see positive RFP outcomes or maintenance of the long-term 5-7% growth target as significantly detracting from our call, as most of the benefits would occur past 2015. We are instead positioning for more disappointment in the form of 2014 EPS guidance and potential incremental equity needs as well as ongoing MN regulatory risk and are downgrading to UW.

- **Lower growth, higher capital spend more likely in near term.** Following the MN case and increased generation buildout, particularly wind in 2014 and 2015, we see the near-term path as one of lower EPS growth and higher capital needs. With the introduction of a 2014-2018 capital plan coming as soon as early November, we see risk of incremental near-term equity needs on top of the \$400MM outstanding ATM. Approximately \$225MM of this has been used so far, and we note as of June 30 Xcel's equity ratio was 45%.
- **2014 growth challenging.** The \$1.99 consensus forecast is little changed over the preceding 6 months and we see risk to the downside. Our \$1.96 estimate implies 3.7% yoy growth, below the long-term 5-7% target.
- **Slower growth not necessarily priced in.** XEL shares have underperformed peers only 3% YTD, mostly in August and leading into the July MN ALJ recommendation. In our opinion, shares are pricing in generally positive results from the generation RFPs and likely continuation of the 5-7% EPS long-term target, without the near-term growth risk.
- **Next MN case won't be much easier.** With seemingly every proposal being a point of contention this year and several important items pushed to next year, we see the first multi-year filing as weighing on shares through at least the start of proceedings early next year.

Electric Utilities

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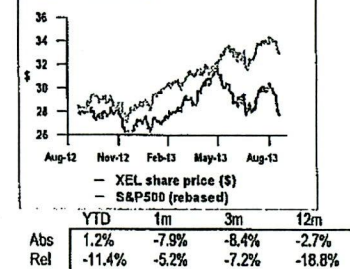
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Price Performance



Xcel Energy Inc. (XEL;XEL US)

FYE Dec	2012A	2013E	2014E (Prev)	2014E (Curr)	2015E
EPS (\$)					
Q1 (Mar)	0.38	0.48A	-	-	-
Q2 (Jun)	0.38	0.40	-	-	-
Q3 (Sep)	0.78	-	-	-	-
Q4 (Dec)	0.29	-	-	-	-
FY	1.85	1.89	1.97	1.96	2.04
Bloomberg EPS FY (\$)	1.80	1.90	-	1.99	2.08

Source: Company data, Bloomberg, J.P. Morgan estimates. Note: 'Bloomberg' above denotes Bloomberg consensus estimates.

Company Data

Price (\$)	27.70
Date Of Price	19 Aug 13
52-week Range (\$)	31.79-25.84
Market Cap (\$ mn)	13,794.60
Fiscal Year End	Dec
Shares O/S (mn)	498
Price Target (\$)	27.00
Price Target End Date	31-Dec-14

See page 4 for analyst certification and important disclosures.

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20 August 2013

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Investment Thesis, Valuation and Risks

Xcel Energy (*Underweight; Price Target: \$27.00*)

Investment Thesis

Xcel offers exposure to a diverse set of integrated electric and gas utilities throughout the Midwest. The company continues to invest heavily in its system and could benefit from several wind and thermal generation projects over the next five years. However, in the near term we see more of a slow growth, higher capital deployment scenario. We are positioning for disappointment in the form of 2014 EPS guidance and potential incremental equity needs as well as ongoing MN regulatory risk into next year.

Valuation

We are downgrading XEL to UW from N and reducing our December 2014 price target to \$27 from \$33. Our price target is derived by applying a discount to the peer group P/E multiple and is based on our 2015E EPS estimate. We feel shares should trade at a discount due to the potential for incremental near-term equity needs and regulatory risk in jurisdictions such as MN.

Risks to Rating and Price Target

- Management's earnings guidance and long-term growth expectations may turn out better than expected, resulting in upside risk for shares.
- Regulated electric and gas utilities are subject to federal and state regulations, including determinations of allowed revenues. Positive changes to the regulatory environments may cause future earnings potential to differ materially from current expectations, including changes to the current negative regulatory sentiment in Minnesota.
- Expected future equity issuance may be lower than expected, resulting in upside risk for shares. The company's current 5 year capital plan anticipates \$400MM in equity, \$235MM of which has already been issued.

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Xcel Energy: Summary of Financials

Income Statement - Annual	FY12A	FY13E	FY14E	FY15E	Income Statement - Quarterly	1Q13A	2Q13E	3Q13E	4Q13E
Sales	10,128	10,521	10,750	11,018	Sales	-	-	-	-
COGS	(4,505)	(4,578)	(4,594)	(4,637)	COGS	-	-	-	-
D&A	(926)	(1,023)	(1,084)	(1,135)	D&A	-	-	-	-
Operations and maintenance	(2,875)	(3,005)	(3,077)	(3,135)	Operations and maintenance	-	-	-	-
Other expenses	-	-	-	-	Other expenses	-	-	-	-
Total operating expenses	8,306	8,607	8,755	8,906	Total operating expenses	-	-	-	-
Other income / (expense)	99	100	95	98	Other income / (expense)	-	-	-	-
EBIT	1,922	2,013	2,090	2,209	EBIT	-	-	-	-
EBITDA	2,848	3,037	3,174	3,344	EBITDA	-	-	-	-
Interest expense	(566)	(547)	(567)	(593)	Interest expense	-	-	-	-
Income tax provision	(450)	(533)	(535)	(567)	Income tax provision	-	-	-	-
Tax rate	33.2%	36.4%	35.1%	35.1%	Tax rate	-	-	-	-
Discontinued operations and other	0	0	0	0	Discontinued operations and other	-	-	-	-
Preferred dividends	0	0	0	0	Preferred dividends	-	-	-	-
Net income	905	933	988	1,049	Net income	-	-	-	-
Total non-recurring items	-	-	-	-	Total non-recurring items	-	-	-	-
Net Income (Recurring)	905	933	988	1,049	Net Income (Recurring)	-	-	-	-
Diluted shares outstanding	488	494	505	513	Diluted shares outstanding	-	-	-	-
Diluted EPS	1.85	1.89	1.96	2.04	Diluted EPS	0.48A	0.40	-	-
DPS (\$)	1.07	1.11	1.16	1.20	DPS (\$)	-	-	-	-
Payout ratio	57.7%	58.9%	59.1%	58.9%	Payout ratio	-	-	-	-
Balance Sheet and Cash Flow Data	FY12A	FY13E	FY14E	FY15E	Ratio Analysis	FY12A	FY13E	FY14E	FY15E
Cash and cash equivalents	82	0	0	0	Sales growth	(4.9%)	3.9%	2.2%	2.5%
Current assets	2,625	2,543	2,543	2,543	EBITDA growth	3.1%	6.6%	4.5%	5.4%
PP&E	23,809	25,941	27,882	29,307	EBIT growth	2.6%	4.8%	3.8%	5.7%
Non-current assets	4,706	4,706	4,706	4,706	Net income (recurring) growth	8.1%	3.0%	6.0%	6.1%
Total assets	31,141	33,190	35,131	36,556	Diluted EPS growth	7.4%	1.9%	3.6%	4.3%
Current liabilities	2,937	3,578	4,759	5,523	Gross margin	55.5%	56.5%	57.3%	57.9%
Long-term Debt	10,144	10,577	10,602	10,652	Operating margin	19.0%	19.1%	19.4%	20.1%
Preferred stock	0	0	0	0	Debt / Capital (book)	54.8%	55.2%	55.9%	56.0%
Other non-current liabilities	9,186	9,472	9,472	9,472	Times interest earned	5.0	5.5	5.6	5.6
Common equity	8,874	9,563	10,298	10,909	ROE	10.4%	10.1%	10.0%	9.9%
Total liabilities & equity	31,141	33,190	35,131	36,556	Return on capital employed (ROCE)	6.9%	6.3%	6.1%	6.0%
Net Income	905	933	988	1,049					
D&A	944	1,023	1,084	1,135					
Change in working capital	(392)	0	0	0					
Change in other assets	40	0	0	0					
Net operating cash flow	2,005	2,243	2,072	2,184					
Cash flow from investing activities	(2,333)	(3,155)	(3,025)	(2,560)					
Net common equity issued/(repurchased)	(34)	305	330	180					
Net debt issued/(repurchased)	870	450	0	0					
Common dividends paid	(487)	(549)	(584)	(617)					
Other financing activity	0	0	0	0					
Cash flow from financing activities	350	206	(254)	(437)					
Increase/(decrease) in cash	22	(706)	(1,206)	(814)					
Cash at beginning of the period	61	82	0	0					
Cash at end of the period	82	(0)	(0)	(0)					

Source: Company reports and J.P. Morgan estimates.
Note: \$ in millions (except per-share data). Fiscal year ends Dec

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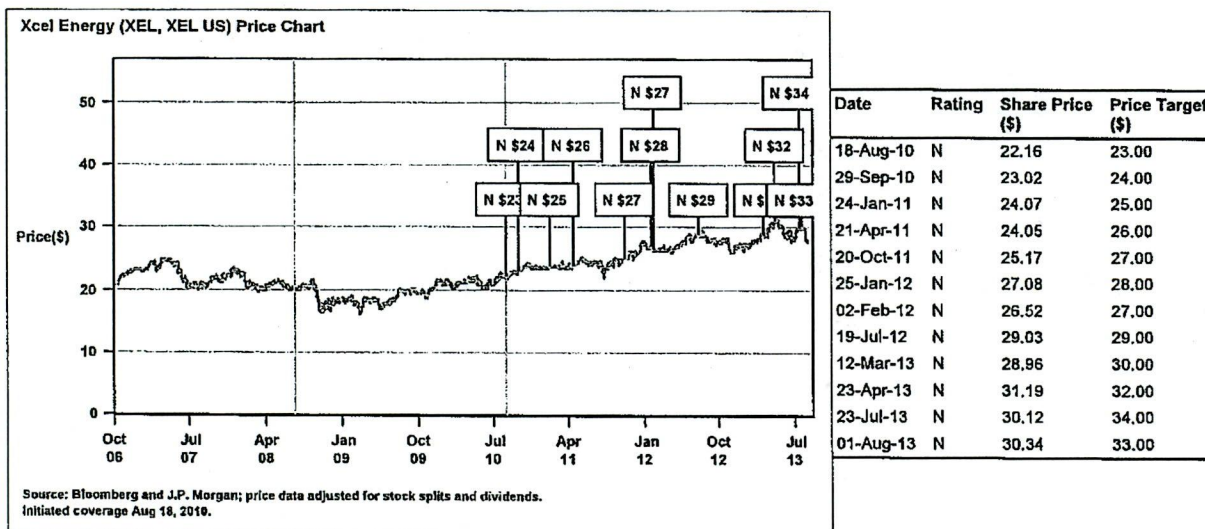
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