



# The Utility Industry: Capital Markets Outlook

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## Who we are:

**With roots tracing to 1832, Janney is a Philadelphia-based full service financial services firm, owned by Penn Mutual Life Insurance Company (\$142.1 billion in life insurance in-force as of year-end 2017).**

**Janney has 120 U.S. locations, with more than 800 financial advisors and more than 200 capital markets professionals. Total employees exceeds 1,900.**

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### Capital Markets Capabilities

#### Equities



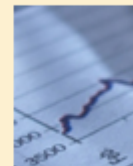
Our success is rooted in our industry knowledge, focused research and client-centered approach to sales and trading.

#### Investment Banking



We provide our clients access to the public and private capital markets, and offer comprehensive M&A advisory services.

#### Fixed Income



We provide clients with exceptional and broad-based access to the global fixed income markets.

## Our Utility Coverage Universe

Ticker	Name	Rating	Price	Fair Value	Upside	18 EPS/(P/E)	19 EPS/(P/E)	20 EPS/(P/E)
<b>WATER UTILITIES</b>								
AWR	American States Water Company	Neutral	\$71.02	\$58.00	-18%	\$1.73 (41.1)	\$2.02 (35.2)	\$2.13 (33.3)
AWK	American Water Works Company, Inc.	Buy	\$106.78	\$102.00	-4%	\$3.30 (32.4)	\$3.58 (29.8)	\$3.91 (27.3)
WTR	Aqua America, Inc.	Buy	\$37.12	\$41.00	10%	\$1.38 (26.9)	\$1.49 (24.9)	\$1.63 (22.8)
CWCO	Consolidated Water Co. Ltd.	Buy	\$12.83	\$16.00	25%	\$0.68 (18.9)	\$0.71 (18.1)	\$0.76 (16.9)
CWT	California Water Service Group	Neutral	\$53.73	\$42.00	-22%	\$1.25 (43.0)	\$1.39 (38.7)	\$1.56 (34.4)
MSEX	Middlesex Water Company	Neutral	\$56.52	\$58.00	3%	\$1.96 (28.8)	\$2.05 (27.6)	\$2.14 (26.4)
SBS	Companhia de Saneamento Basico do Estado	Neutral	\$10.31	\$9.18	-11%	\$0.79 (13.1)	\$1.05 (9.8)	\$1.14 (9.1)
SBSP3-BR	Companhia de Saneamento Basico do Estado	Neutral	R\$40.12	\$35.00	-13%	\$3.01 (13.3)	\$4.02 (10.0)	\$4.34 (9.2)
SJW	SJW Group	Buy	\$63.04	\$64.00	2%	\$1.82 (34.6)	\$2.30 (27.4)	\$2.45 (25.7)
<b>ELECTRIC &amp; GAS UTILITIES</b>								
AGR	Avangrid, Inc.	Neutral	\$50.04	\$50.00	0%	\$2.21 (22.6)	\$2.30 (21.8)	\$2.50 (20.0)
CPK	Chesapeake Utilities Corporation	Neutral	\$92.19	\$86.00	-7%	\$3.31 (27.9)	\$3.66 (25.2)	\$3.93 (23.5)
ES	Eversource Energy	Buy	\$71.69	\$74.00	3%	\$3.25 (22.1)	\$3.45 (20.8)	\$3.69 (19.4)
NJR	New Jersey Resources Corporation	Buy	\$49.71	\$51.00	3%	\$2.74 (18.1)	\$2.01 (24.7)	\$2.22 (22.4)
RGCO	RGC Resources, Inc.	Neutral	\$26.68	\$28.00	5%	\$0.95 (28.1)	\$1.02 (26.2)	\$1.11 (24.0)
SJI	South Jersey Industries, Inc.	Buy	\$31.70	\$34.00	7%	\$1.38 (23.0)	\$1.05 (30.2)	\$1.61 (19.7)
UGI	UGI Corporation	Buy	\$55.69	\$65.00	17%	\$2.74 (20.3)	\$2.70 (20.6)	\$3.10 (18.0)
UTL	Unitil Corporation	Buy	\$53.62	\$54.00	1%	\$2.23 (24.0)	\$2.30 (23.3)	\$2.45 (21.9)
<b>MLPs</b>								
APU	AmeriGas Partners, L.P.	Neutral	\$29.50	\$35.00	19%	#N/A	\$2.42 (12.2)	\$2.59 (11.4)

Sources: FactSet (pricing), Janney Montgomery Scott, LLC Ratings/Estimates/Fair Values

# The Macro View – Interest Rates & the Economy

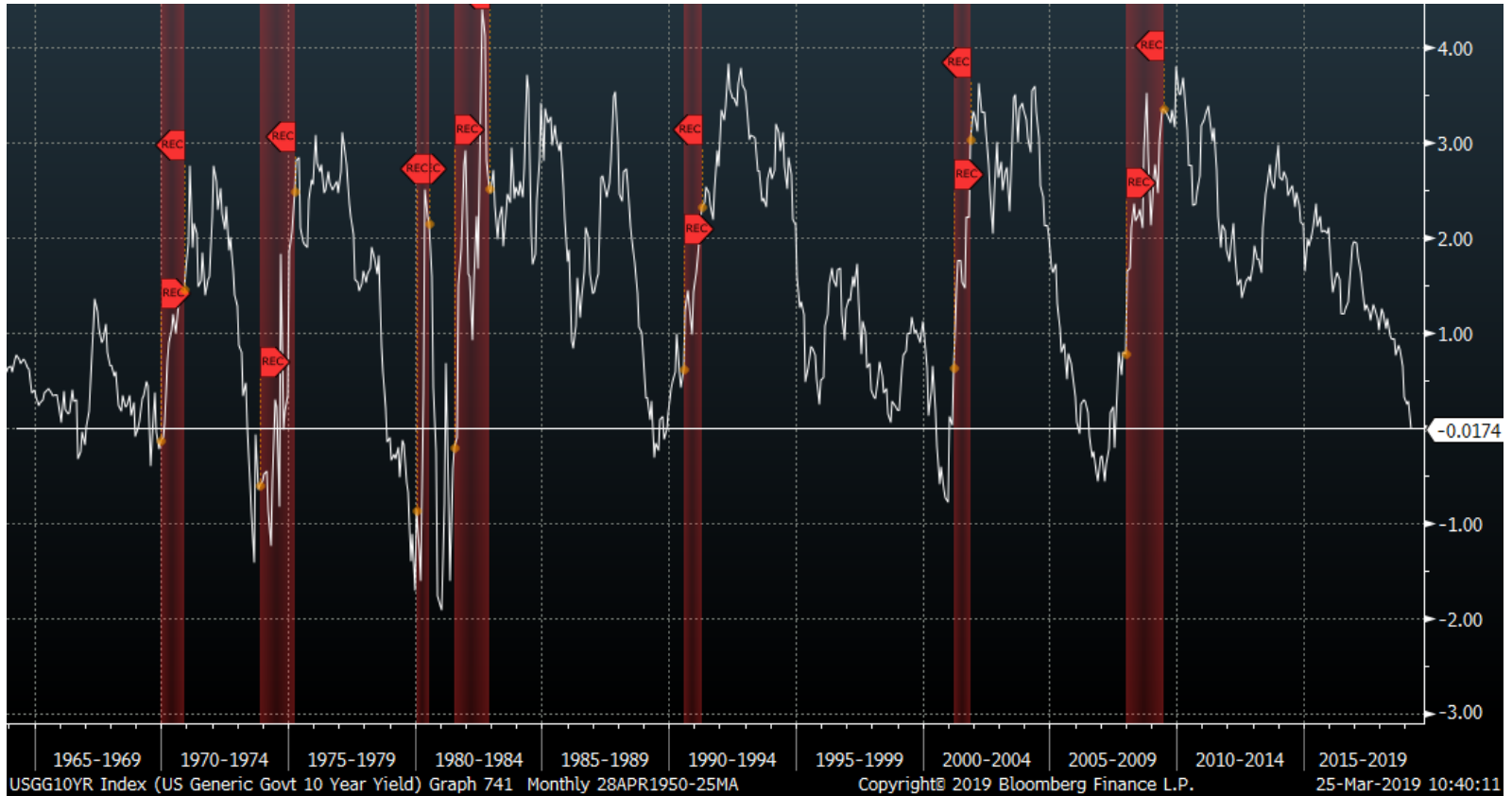
## 10 Year Yields



Sources: FactSet

# The Macro View – Interest Rates & the Economy

## Yield Curve vs. Prior Recessions



Sources: Bloomberg

## Utility Stocks Have Enjoyed a Long, Uninterrupted Run Higher

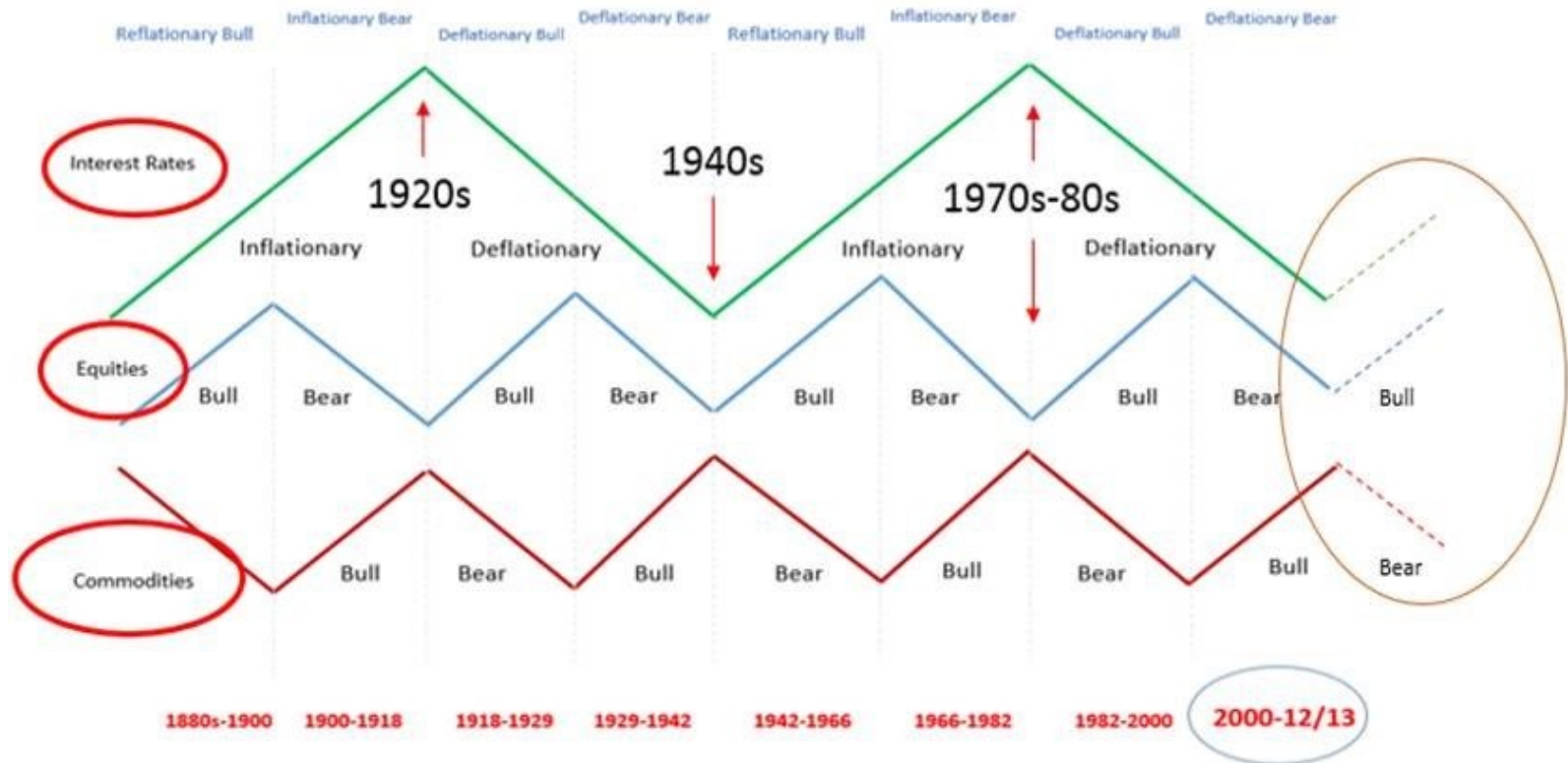


Source: FactSet Research Systems, Inc.

Janney Montgomery Scott LLC > JANNEY\_RES > PERSONAL:Janney Research Workspace\_2016 > Coverage List > Watchlist

# The Macro View – Interest Rates & the Economy

## Long Cycle Model Implies Equity Bull Market



Source: Janney Montgomery Scott

## The Short/Medium Term Outlook

**Interest Rate Environment Remains Supportive:** With a potential recession looming, the Federal Reserve has gone from 4 anticipated rate hikes in 2019 to 0. 10-year yields have been moving lower, with utility stocks pushing up against all-time highs in terms of valuation multiples. The next move by the Federal Reserve appears to be lower versus higher. Interest rates could remain accommodative for several more years.

**Valuation Multiples are Likely to Continue Expanding:** The “safe haven” nature of utilities should continue to attract investors until sustained, higher interest rates materialize, given utility dividends typically increase, while most fixed income payouts remain fixed.

**Regulators and Authorized ROE's Remain the Wildcard:** Constructive regulatory jurisdictions are incentivizing utilities to invest in infrastructure while interest rates and natural gas prices are low. Ratepayers are benefitting from low natural gas prices both in the generation part of their electric bills (where NG is used significantly for generation) and also for residential heating and other uses. That said, less constructive environments are squeezing ROE's lower and redeploying ratepayer savings into other areas. WHERE a utility operates remains very important from an investment perspective.



## The Long-Term Outlook

**Interest Rates Likely to Rise:** The U.S. has significant debt and budget deficit problems that are not being addressed. Creditors are likely to demand higher returns to accept those risks.

**Valuation Multiples Could Contract:** Both utilities and regulators should expect an eventual “reckoning” brought on by higher interest rates, and seek to minimize the damage to equity values that could bring. Reduction in regulatory lag to pass-through higher rates to customers and a willingness to increase ROE’s would seem to be logical pathways when the time arrives.

**Rate Cases May Be More Challenging:** The recent past and near/medium-term look to be some of the best for utilities, with constructive environments encouraging investment in systems while capital is cheap. That likely changes longer-term when capital becomes more expensive. Earnings growth could slow at the very time pressure to increase dividends materializes.

# Disclosures



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**BUY:** Janney expects that the subject company will appreciate in value. Additionally, we expect that the subject company will outperform comparable companies within its sector.

**NEUTRAL:** Janney believes that the subject company is fairly valued and will perform in line with comparable companies within its sector. Investors may add to current positions on short-term weakness and sell on strength as the valuations or fundamentals become more or less attractive.

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### Janney Montgomery Scott Ratings Distribution as of 12/31/18

#### IB Serv./Past 12 Mos.\*

Rating	Count	Percent	Count	Percent
<b>BUY [B]</b>	107	55.44	24	22.43
<b>NEUTRAL [N]</b>	86	44.56	18	20.93
<b>SELL [S]</b>	0	0.00	0	0.00

\*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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