



March 30, 2015

**CURRENT PRICE:** \$75.90  
**RATING:** BUY  
**PRICE TARGET:** \$88  
**CURRENT YIELD:** 4.2%

**EPS Estimates - Non-GAAP**

	DEC 14A	DEC 15E
1Q	\$1.17	\$0.74
2Q	\$1.11	\$0.97
3Q	\$1.41	\$1.66
4Q	\$0.86	\$1.31
	<b>\$4.55</b>	<b>\$4.68</b>

**Trading Data**

52-WEEK PRICE RANGE: **\$89.97 - \$68.61**  
 SHARES OUTSTANDING: **707(M)**  
 MARKET CAP: **\$53,661(M)**  
 AVG. DAILY TRADING VOLUME: **4.0(M)**  
 S&P 500: **2,086**

**Valuation Data**

BOOK VALUE: **\$57.82**  
 PRICE TO BOOK: **1.46x**  
 DIVIDEND: **\$3.18**

**Duke Energy (NYSE: DUK)**

*4Q14 earnings results- maintain BUY rating*

**Highlights**

- Adjusted diluted earnings of \$0.86/share vs. \$1.00 /share
- Higher O&M expenses hurt Regulated's results
- Bringing overseas money to US
- Provided 2015 earnings guidance range of \$4.55-\$4.75/share
- Maintain BUY rating

**Investment Thesis**

Wall Street believes the US economy is emerging from its recent economic malaise with GDP estimated to grow about 2%-3% over the next year or two. While we find this difficult to predict, we believe investors should consider investing in sectors where revenue streams are fairly predictable, with attractive dividend yields, low valuations, and earnings growth potential when the US economy emerges from this malaise. One attractive sector is the utility group and one company in this area we like Duke Energy. This utility pays an attractive 4.2% dividend yield, has potential dividend growth, and offers earnings growth potential going forward. DUK is rated BUY and our price target is \$88/share.

**Company Summary**

Duke Energy, headquartered in Charlotte NC, is one of the largest energy providers in the US. The company is comprised of three business units; Regulated Utilities (RU), Commercial Power (CP), and Duke Energy International (IE). USFE&G contains the company's regulated generation and the electric/gas distribution and transmission systems. Serving approximately 7.2 million electric customers in NC, SC, FL, IN, OH, and KY. USFE&G operates 150,900 miles of electric distribution lines and a 20,900-mile transmission system. USFE&G owns approximately 49,000 megawatts (MW) of regulated electrical generating capacity with its plants fueled by coal, oil, natural gas, hydroelectric, and nuclear. This past July DUK recently merged with Progress Energy creating one of the largest electric utilities in the US.

*For Important Disclosure information regarding the Firm's rating system, valuation methods and potential conflicts of interest, please refer to the last two pages of this report.*

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# EQUITY RESEARCH

## Recent Earnings

DUK reported 4Q14 diluted earnings of \$0.14/share vs. \$0.97/share during 4Q13. The decline, when comparing the two quarters, was due to lower operating income in the Regulated Utilities(RU) and International Energy(IE) units, which were partly offset by lower losses at the Commercial Power Unit (CP). Additionally, 4Q14 per share results were negatively impacted by an internal tax adjustment charge (-\$0.53/share), a litigation reserve charge for the NC ash clean-up (-\$0.14/share), costs to achieve the Progress Energy merger (-\$0.03/share), and a discontinued operations charge (-\$0.02/share). FY14 reported diluted earnings increased to \$4.55/share from \$4.36/share. Adjusted 4Q14 diluted earnings decreased to \$0.86/share vs. \$1.00/share during 4Q13 due to higher RU operation/maintenance expenses related to nuclear outage cost levelization in the Carolinas and timing of fossil plant outages. IP's lower operating results, from the Brazilian drought, were more than offset higher PJM capacity revenues for the Midwest Generation fleet. Adjusted diluted earnings for FY14 decreased to \$2.66/share from \$3.76/share.

## QUARTERLY SEGMENT RESULTS

The Regulated Utility segment's reported adjusted segment income declined to \$551 million from \$607 million, equating to a decrease of \$0.08/share. The results were impacted by higher operations/maintenance expense primarily due to nuclear outage cost levelization and the timing of fossil plant outages (-\$0.10/share). Operating revenues rose to \$5.20 billion from \$5.14 billion, while operating expenses increased to \$4.22 billion from \$3.99 billion. These factors caused operating income to decrease to \$980 million from \$1.16 billion.

Total GWh rose slightly to 58,271 GWh from 58,208 GWh. The increase was due to higher Duke Energy Progress GWh sales (+7.2%), outpacing declines from Duke Energy Carolina (-1%), Duke Energy Indiana (-7.6%), and Duke Energy Ohio (-0.3%), while Duke Energy Florida was flat.

CP reported adjusted segment income of \$32 million vs. \$3 million, equating to an increase of \$0.05/share. The improved results were due to higher profits from the Midwest coal and gas generation fleet (+\$0.02/share) produced from increased PJM capacity prices, which were partly offset by increased outage costs. Additionally, the renewable business added to CP's segment income (+\$0.02/share) because of lower costs and additional renewable investments. Operating revenues declined to \$60 million from \$71 million, and operating expenses declined to \$86 million from \$117 million, allowing the operating loss to fall to -\$26 million from -\$70 million. Actual GWh plant production was flat at 1,349 GWh vs. 1,350 GWh.

IP reported adjusted segment income of \$72 million vs. \$108 million, a decrease of \$0.05/share. The decrease was due to unfavorable results in the Latin American operations (-\$0.06/share) caused by lower volumes and higher purchased power costs from the continuing drought in Brazil. Operating revenues declined to \$306 million from \$378 million, and operating expenses rose to \$247 million from \$235 million, causing operating income to fall to \$58 million from \$146 million. Given the operating conditions in Latin America, GWh sales declined 13.5% to 4,815 GWh.



Other, which includes corporate interest expense not allocated to the other units, DUK's captive insurance company, other investments, and income tax levelization adjustments generated -\$45 million in net expense vs. a net expense of \$5 million. This equated to a decrease of \$0.06/share caused mainly by income tax levelization adjustments.

## RECENT DEVELOPMENTS

DUK plans to appeal the \$25.1 million fine, by NC environmental regulators, related to water contamination from two coal ash pits at the retired Sutton power plant near Wilmington NC. The company plans to file a formal appeal with NC's Office of Administrative Hearings by 4/9/15. DUK stated its intent to close 32 ash basins throughout NC after receiving state wastewater permits.

DUK agreed to settle a shareholder lawsuit, for \$146 million, regarding the 2012 purchase of Progress Energy. Previously, DUK had taken a \$26 million charge, related to the matter, and insurance will cover the remaining \$120 million of the settlement.

The company also reached a \$102 million settlement with the US Government creating an end to the criminal investigation regarding last year's Dan River coal ash spill. Under the agreement, DUK will pay \$68 million in fines and \$34 million for community service/mitigation. Payments will be borne by shareholders and not DUK's customers.

DUK recently completed a strategic review of its international operations and decided to continue to holding the business units. The Board of Directors approved an annual dividend increase of approximately 2%.

Dynegy (DYN-\$30.88) received FERC approval to buy power plants in Illinois, Ohio, and Pennsylvania from DUK and Energy Capital Partners for \$6.25 billion.

During 4Q14 DUK declared a \$2.7 billion taxable dividend in the form of notes payable related to historical undistributed earnings from overseas. This will allow the company to bring this money into the US. As a result, DUK recognized a \$373 million US income tax charge during 4Q14 and expects to remit \$1.2 billion-\$1.4 billion in 2015, and management anticipates the remaining amount will be remitted by 2022. The company presently has \$1.7 billion of offshore cash. DUK does not expect to be a significant cash payer on these monies "until the 2018 timeframe". Additionally, the company expects to use cash generated from its international operations to be used primarily to pay off the notes of the parent company, Duke Energy, with the remainder going towards reinvestment in the international business.



## Our Thoughts

Factoring out the charges incurred during 4Q14 (\$0.70/share), DUK reported diluted earnings of \$0.14/share vs. \$0.97/share during 4Q13. Adjusted 4Q14 diluted earnings decreased to \$0.86/share vs. \$1.00/share during 4Q13 due to higher RU operation/maintenance expenses related to nuclear outage cost levelization in the Carolinas and timing of fossil plant outages. The RU and IP units reported lower operating income while CP reported a lower operating loss when comparing 4Q14 and 4Q13. Going forward, the regulated units offers a steady stream of business, while the company will still need to deal with litigation issues created by the ash spill into NC waterways, and improve results at DUK's IP & CP's operating units.

We continue to rate DUK a BUY and is recommended for income/growth investors. The Board of Directors recently increased the annual dividend approximately 2%. Given, DUK's 2015 adjusted earnings guidance of \$4.55-\$4.75/share, and goal of growing long term annual earnings by 4%-6%, shareholders may receive further dividend increases in the future. Our price target is \$88/share, equating to 1.52x book value.



## Risks

There is no guarantee DUK will improve earnings/cash flow. Declining US electric sales volumes may hurt the company's revenues and profits. Rising interest rates, higher fuel prices, negative rate case decisions, tax issues, or rising operating costs could negatively impact DUK's earnings. DUK's stock may be adversely impacted by negative equity/credit markets, terrorist attacks, and failure to comply with Sarbanes Oxley guidelines.

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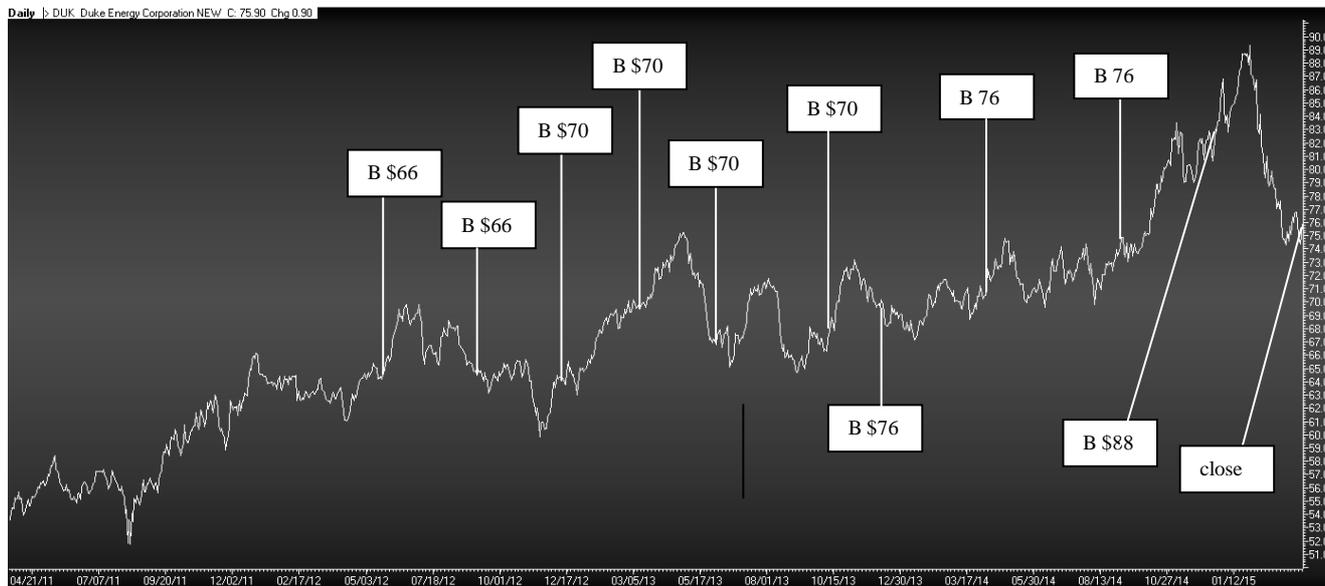
# EQUITY RESEARCH

Duke Energy  
Condensed Consolidated Statements of Operations  
unaudited  
(in millions, except per share amounts)

	1Q14	2Q14	3Q14	4Q14	2014	1Q15e	2Q15e	3Q15e	4Q15e	2015e
<b>Operating Revenues:</b>										
Regulated electric	\$5,578	\$5,167	\$5,861	\$4,944	\$21,550	\$5,469	\$5,388	5,948	\$5,286	\$22,091
Non-regulated electric/hatgas/other	824	675	449	144	1,802	840	972	852	940	3,604
Regulated natural gas	222	107	85	159	573	205	112	88	163	568
Total Operating revenues	6,624	5,949	6,395	4,957	23,925	6,514	6,472	6,888	6,389	26,263
<b>Operating Expenses:</b>										
Fuel electric gen. & purchased power-reg	2,000	1,808	2,132	1,746	7,686	2,015	1,923	1,786	1,703	7,427
Fuel electric gen. & purch power-non reg	409	436	148	460	533	443	452	381	483	1,759
Cost of natural gas & coal sold	122	43	27	56	248	118	114	39	71	342
Operation, maintenance, & other	1,506	1,467	1,409	1,474	5,856	1,498	1,526	1,455	1,427	5,906
Depreciation & Amortization	790	761	788	728	3,066	785	791	785	752	3,113
Property & other taxes	358	318	275	262	1,213	352	336	324	315	1,327
Impairment charges	1,382	6	1	1,470	81	3	25	8	2	38
Total Operating expenses	6,567	4,839	4,780	2,497	18,683	5,214	5,147	4,778	4,753	19,892
Gains/losses sale of other assets (net)	1	6	4	5	16					
Operating Income	58	1,116	1,619	2,465	5,258	1,300	1,325	2,109	1,636	6,370
<b>Other Income/Expenses</b>										
Equity in earnings of unconsolidated affiliates	36	33	28	33	130	38	23	32	26	119
Impairments/Gains on unconsol affiliates sales				17	17		2			2
Other Income/Expenses	95	89	109	58	351	95	48	43	35	221
Total other income/expenses	131	122	137	108	498	133	73	75	61	342
<b>Interest expense</b>										
Income from Cont Ops before Income Taxes	406	413	405	398	1,622	402	399	407	404	1,612
Income tax expense	-217	825	1,351	516	2,775	765	853	1,777	1,293	4,688
Income from Cont Ops before Income Taxes	-127	209	460	1,127	1,669	245	171	568	414	1,398
Income from Discontinued Ops, net of Taxes	-80	616	891	1,948	2,465	520	682	1,209	879	3,290
Income from Discontinued Ops, net of Taxes	-3	-3	378	948	-576	-6	-3	-4	-4	-17
<b>Net Income</b>										
Net Income	-93	613	1,269	100	1,889	514	679	1,205	875	3,273
Net Income/loss attributable to non-controlling interest	-4			10	6	-5	-4			-9
Net Income attributable to Duke Energy Corp	(\$97)	\$609	\$1,274	\$97	\$1,883	\$509	\$675	\$1,205	\$875	3,264
<b>Diluted EPS</b>										
Diluted EPS	(\$0.14)	\$0.86	\$1.80	\$0.14	\$2.66	\$0.72	\$0.96	\$1.55	\$1.24	\$4.47
Net Income from discon ops attributable shareholders	(\$0.14)	\$0.86	\$1.80	\$0.14	\$2.66	\$0.72	\$0.96	\$1.55	\$1.24	\$4.47
Diluted EPS	(\$0.14)	\$0.86	\$1.80	\$0.14	\$2.66	\$0.72	\$0.96	\$1.55	\$1.24	\$4.47
Adjustments	\$1.31	\$0.25	(\$0.40)	\$0.72	\$1.89	\$0.02	\$0.01	\$0.11	\$0.07	\$0.21
Adjusted Diluted EPS	\$1.17	\$1.11	\$1.40	\$0.86	\$4.55	\$0.74	\$0.97	\$1.66	\$1.31	\$4.68

## Important Disclosures

Daily | DUK Duke Energy Corporation NEW | C: 75.90 Chg 0.50



12/26/14 Raise Price Target to \$88  
 12/6/13 Raise Price Target to \$76  
 12/12/12 Raise Price Target to \$70  
 12/5/11 Raise Price Target to \$66  
 9/19/11 Raise Price Target to \$61.50  
 9/23/09 Initiate Buy Rating & \$60 Target Price

Ratings:  
 Buy: B  
 Hold: H  
 Sell: S

\$88 price target equates to 1.52x book value/share

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