



December 17, 2015

CURRENT PRICE: \$70.50
RATING: BUY
PRICE TARGET: \$88
CURRENT YIELD: 4.7%

EPS Estimates - GAAP

	DEC 14A	DEC 15E
1Q	\$1.17	\$1.22A
2Q	\$1.11	\$0.95A
3Q	\$1.40	\$1.47A
4Q	\$0.86	\$0.97
	\$4.55	\$4.61

Trading Data

52-WEEK PRICE RANGE: **\$89.97 - \$65.50**
 SHARES OUTSTANDING: **688(M)**
 MARKET CAP: **\$48,524(M)**
 AVG. DAILY TRADING VOLUME: **3.4(M)**
 S&P 500: **2,041**

Valuation Data

BOOK VALUE: **\$57.92**
 PRICE TO BOOK: **1.22x**
 DIVIDEND: **\$3.30**

Duke Energy (NYSE: DUK)

3Q15 earnings results- maintain BUY rating

Highlights

- Adjusted diluted earnings of \$1.47/share vs. \$1.40 /share
- Regulated unit improves profits and International's declines
- Announced purchase of Piedmont Natural Gas
- Narrowed 2015 adjusted earnings guidance to \$4.55-\$4.65/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 4.7% 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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Recent Earnings

DUK reported 3Q15 diluted earnings of \$1.35/share vs. \$1.80/share during 4Q14. Last year's 3Q14 results included a \$0.43/share favorable adjustment for a change in the estimated value of DUK's Midwest generation business. 3Q15's adjusted diluted earnings were \$1.47/share vs. \$1.40 share during 4Q15. The improved results were due to warmer weather in 3Q15 vs. 3Q14, and strong growth in the Regulated Utilities unit which included the positive impact of DUK's recent acquisition of the NC Eastern Municipal Power Agency (NCEMPA). These positives were partly offset by weakness in the International unit. Results were also positively impacted, adding \$0.04/share, by the completion of the \$1.5 billion share repurchase program associated with the sale of the Midwest Generation business to Dynegy, (DYN-\$10.25).

SEGMENT RESULTS

Regulated Utilities unit produced 3Q15 adjusted segment income of \$965 million vs. \$920 million during 3Q14. The improvement was due to warmer weather in its service region (+\$0.09/share), higher revenues from increased pricing/riders resulting from improved energy efficiency programs, as well as prior year tune-ups lacking this year (+\$0.07/share), and increased margins in the wholesale business -including NCEMPA addition (+\$0.05/share). These positives were partly offset by higher O&M expense (-\$0.06/share) related to outage timings, increased cost related to NCEMPA, and higher storm costs, in addition to a higher effective tax rate (-\$0.04/share).

When comparing the two quarters, total GWh sales grew 5.2% to 69,015 GWh from 65,600 GWh. The increase was due to higher GWh sales from Duke Energy Carolinas (+4.0%), Duke Energy Progress (+10.5%), Duke Energy Ohio (+3.6%), and Duke Energy Indiana (+6.8%). These gains were partly offset by a decrease from Duke Energy Florida (-0.3%).

IE reported 3Q15 adjusted segment income of \$69 million vs. \$80 million during 3Q14. The decrease was due to unfavorable currency exchange rates related to Brazil and an asset impairment in Ecuador (-\$0.01/share) and lower margins at National Methanol. (-\$0.01/share). These were partly offset by lower purchase costs in Brazil. The commercial portfolio incurred \$0.08/share of lower adjusted earnings resulting from the absence of 3Q14's Midwest Generation profits. IE's GWh sales 6.9% to 4,590 GWh from 4,292 GWh.

CP produced 3Q15 adjusted segment of -\$4 million vs. \$51 million during 3Q14. The decrease in results was due mainly to the sale of the Midwest Generation assets to Dynegy (DYN-\$10.25) this past April. Renewable plant GWh production increased 16.7% to 1,230 GWh from 1,054 GWh.

Other, includes corporate interest expense not allocated to the business units, results from Duke Energy's captive insurance company, other investments, and quarterly income tax levelization adjustments. This unit reported net expense of \$19 million vs. \$58 million in next expense when comparing 3Q15 vs. 3Q14. This equates to an improvement of \$0.06/share when excluding the effect of the recent accelerated stock repurchase program. 3Q15's



improvement came mainly from a prior year tax charge and quarterly tax levelization, including the recognition of renewable tax credits.

RECENT DEVELOPMENTS

DUK announced it was buying Piedmont Natural Gas (PNY-\$57.17) for \$60/share. PNY shareholders will get \$60/share in cash and DUK will assume approximately \$1.8 billion of PNY's debt. Expectations are for the deal to close by year-end 2016, assuming it receives regulatory approval.

Duke Energy proposed building two new solar projects in NC. One is a 60 MW plant near Monroe NC and the other is a 15.4 MW plant in Mocksville NC. Both would be owned/operated by DUK.

The company's Indiana unit filed a revised seven-year, \$1.83 billion plan, with state regulators to upgrade the electric grid in its service area to update infrastructure and improve service reliability for the 800,000 customer base.

Plans were cancelled to build a 45-mile power line across the Carolina mountains to an Ashville NC power plant and instead DUK will replace the coal-fired plant by 2020 with two smaller gas units.

DUK reached a settlement to end a class-action lawsuit alleging the utility gave improper rebates to some of its largest Ohio electric customers. The amount of settlement was \$81 million and DUK said shareholders, not customers, would cover the cost of the agreement.

A deal was reached between DUK and NC's Department of Environmental Quality where the company will pay \$7 million to resolve claims related to groundwater contamination at its NC coal ash facilities. NC said this agreement also implements accelerated remediation costs estimated to be an additional \$10 million-\$15 million.

The owners of the Atlantic Coast Pipeline, consisting of DUK, Dominion Resources (D-\$67.54), AGL Resources (GAS-\$63.10), and Piedmont Natural Gas (PNY-\$57.17), applied with FERC to build the proposed pipeline. Estimates place pipeline construction starting in 2H16 and completion/full-operation by 4Q18.

DUK completed the announced \$1.5 billion accelerated stock repurchase program associated with the recent sale of its Midwest Generation assets to Dynegy Corp. (DYN-\$10.25). The program retired approximately 19.8 million shares of DUK's common stock.



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Our Thoughts

A decent 3Q15 earnings report as DUK generated 3Q15 diluted earnings of \$1.35/share vs. \$1.80/share during 4Q14. Last year's 3Q14 results included a \$0.43/share favorable adjustment for a change in the estimated value of DUK's Midwest generation business. 3Q15's adjusted diluted earnings were \$1.47/share vs. \$1.40 share during 4Q15. The improved results were due to warmer weather in 3Q15 vs. 3Q14, and strong growth in the Regulated Utilities unit which included the positive impact of DUK's recent acquisition of the NC Eastern Municipal Power Agency (NCEMPA).

During its earnings conference call, management narrowed its 2015 adjusted diluted earnings guidance range to \$4.55-4.65/share from \$4.55-\$4.75/share. Further, DUK expressed hopes its International units profits, declining of late, could bottom out in 2016 at approximately \$0.30/share for the full year and potentially pivot higher in 2017-2018 based on the materialization of certain operating/currency improvements. Management expects further growth of its low-risk utility business and expects the PNY acquisition will increase DUK's natural gas foot print, raise its Atlantic Coast Pipeline ownership to 50%, triple the number of gas customers, and be accretive to earnings in 2017. This stock is recommended for income/growth investors given DUK's current dividend yield of 4.7% and the potential of future dividend increases based on increasing adjusted diluted earnings. We rate DUK a BUY and our price target is \$88/share, equating to 1.52x book value per share.



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

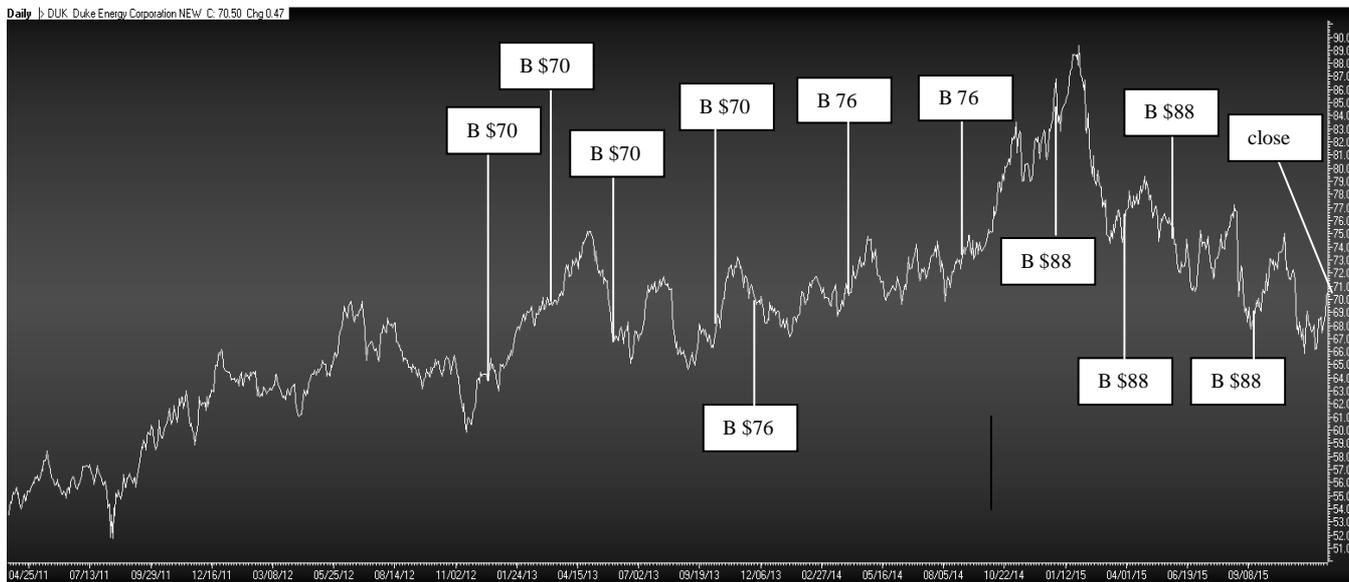
	1Q14	2Q14	3Q14	4Q14	2014	1Q15	2Q15	3Q15	4Q15e	2015e
Operating Revenues:										
Regulated electric	\$5,578	\$5,167	\$5,861	\$4,944	\$21,550	\$5,457	\$5,090	6,017	\$5,286	\$21,850
Non-regulated electric/natgas/other	824	675	449	144	1,802	377	403	377	940	2,097
Regulated natural gas	222	107	85	159	573	231	96	89	163	579
Total Operating revenues	6,624	5,949	6,395	4,957	23,925	6,065	5,589	6,483	6,389	24,526
Operating Expenses:										
Fuel electric gen. & purchased power-reg	2,000	1,808	2,132	1,746	7,686	1,941	1,721	2,113	1,703	7,478
Fuel electric gen. & purch power-non reg	409	436	148	460	533	104	118	61	483	766
Cost of natural gas & coal sold	122	43	27	56	248	111	26	21	71	229
Operation, maintenance, & other	1,506	1,467	1,409	1,474	5,856	1,426	1,422	1,426	1,427	5,701
Depreciation & Amortization	790	761	788	728	3,066	777	790	774	752	3,093
Property & other taxes	358	318	275	262	1,213	264	279	293	315	1,151
Impairment charges	1,382	6	1	1,470	81			111	2	113
Total Operating expenses	6,567	4,839	4,780	2,497	18,683	4,623	4,356	4,799	4,753	18,531
Gains/losses sale of other assets (net)	1	6	4	5	16	14	13	4		31
Operating Income	58	1,116	1,619	2,465	5,258	1,456	1,246	1,688	1,636	6,026
Other Income/Expenses										
Equity in earnings of unconsolidated affiliates	36	33	28	33	130	13	23	17	26	79
Impairments/Gains on unconsol affiliates sales				17	17					
Other Income/Expenses	95	89	109	58	351	74	72	57	35	238
Total other income/expenses	131	122	137	108	498	87	95	74	61	317
Interest expense										
Income from Cont Ops before Income Taxes	406	413	405	398	1,622	403	403	402	404	1,612
Income tax expense	-217	825	1,351	516	2,775	1,140	938	1,360	1,293	4,731
Income from Cont Ops before Income Taxes	-127	209	460	1,127	1,669	364	334	420	414	1,532
Income from Discontinued Ops, net of Taxes	-80	616	891	1,948	2,465	776	604	940	879	3,199
Income from Discontinued Ops, net of Taxes	-3	-3	378	948	-576	91	-57	-5	-4	-25
Net Income										
Net Income/loss attributable to non-controlling interest	-93	613	1,269	100	1,889	867	547	935	875	3,224
Net Income attributable to Duke Energy Corp	-4		10	6		-3	-4	-3	-10	
Net Income attributable to Duke Energy Corp	(\$97)	\$609	\$1,274	\$97	\$1,883	\$864	\$543	\$932	\$875	3,214
Diluted EPS										
Net Income from discon ops attributable shareholders	(\$0.14)	\$0.86	\$1.80	\$0.14	\$2.66	\$1.09	\$0.78	\$1.35	\$1.24	\$4.46
Diluted EPS	(\$0.14)	\$0.86	\$1.80	\$0.14	\$2.66	\$1.09	\$0.78	\$1.35	\$1.24	\$4.46
Adjustments	\$1.31	\$0.25	(\$0.40)	\$0.72	\$1.89	\$0.13	\$0.17	\$0.12	(\$0.27)	\$0.15
Adjusted Diluted EPS	\$1.17	\$1.11	\$1.40	\$0.86	\$4.55	\$1.22	\$0.95	\$1.47	\$0.97	\$4.61



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Important Disclosures

Daily | DUK: Duke Energy Corporation NEW | C: 70.50 | Chg: 0.47



- 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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- (3) Sell – The stock's total return including dividends is expected to be below the industry or market average by 10% or more over the next twelve months.

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