



November 14, 2018

CURRENT PRICE: \$73.65
RATING: HOLD
PRICE TARGET: N/A
CURRENT YIELD: 4.5%

EPS Estimates - Non-GAAP

	DEC 17A	DEC 18E
1Q	\$0.97	\$1.14A
2Q	\$0.67	\$0.86A
3Q	\$1.04	\$1.15A
4Q	\$0.91	\$1.00
	\$3.59	\$4.15

Trading Data

52-WEEK PRICE RANGE: **\$85.30-\$61.53**
 SHARES OUTSTANDING: **655.1(M)**
 MARKET CAP: **\$48,248(M)**
 AVG. DAILY TRADING VOLUME: **3.02(M)**
 S&P 500: **2,702**

Valuation Data

BOOK VALUE: **\$27.58**
 PRICE TO BOOK: **2.67x**
 DIVIDEND: **\$3.34**

Dominion Energy (NYSE: D)

3Q18 Earnings

Highlights

- 3Q18 operating earnings \$1.15/share vs. \$1.01/share during 3Q17
- Selling non-regulated assets to pay down debt
- Still negotiating Scana merger
- Narrowed 2018 operating earnings guidance to \$3.95-\$4.10/share
- Maintain HOLD rating

Company Summary

Dominion Energy, headquartered in Richmond VA, is one of the largest US electric utilities. The company has three operating units: Power Delivery, Power Generation, and Gas Infrastructure. Power Delivery operates D's regulated electric distribution, transmission and un-regulated retail business (gas & electric). Also, it provides electricity to 2.5 million customers in VA/NC. Power Generation operates the electric generation plants for D. Gas Infrastructure operates the natural gas pipeline/storage business and Dominion East Ohio. D recently purchased Questar adding regulated and unregulated gas businesses. On a combined basis, D now has 2.3 million natural gas utility customers in OH, UT, VA, WV, & WY, 1.3 million retail energy/energy related customer accounts in 13 states, 15,000 miles of gas gathering/storage/transmission pipelines and 51,000 miles of gas distribution pipelines. Also, D owns 6,600 miles of electric transmission lines and 26,200 MW of electrical production in 11 states. Since 2003 D has grown its dividend from \$1.29/share to \$3.34/share. 2017's operating earnings decreased to \$3.59/share from \$3.80/share during 2016.

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

D reported 3Q18 operating earnings of \$1.15/share vs. \$1.04/share during 3Q17. The improvement was due to favorable weather in the regulated electric service territory, commercial operation of the Cove Point Liquefaction plant, and the positive impact of the recent tax reform act. These were partly offset by lower renewable energy investment tax credits and higher outstanding shares. 3Q18 GAAP earnings increased to \$1.30/share from \$1.03/share, when comparing the two quarters. Operating revenues improved to \$3.45 billion from \$3.18 billion and operating expenses rose to \$2.30 billion from \$2.02 billion. As a result, EBIT increased to \$1.52 billion from \$1.27 billion.

SEGMENT RESULTS

Power Delivery reported operating income of \$269 million vs. \$283 million. This decrease came from increases in operations/maintenance expense (\$130 million vs. \$109 million), DD&A (\$158 million vs. \$149 million), and other taxes (\$43 million vs. \$42 million). These higher expenses more than offset higher operating revenues (\$601 million vs. \$584 million). Reported segment income rose to \$163 million from \$138 million due to lower taxes. Adjusted EBITDA decreased to \$434 million from \$441 million and Power Delivery's contribution to D's overall earnings rose to \$0.25/share from \$0.21/share.

Total delivered GWh increased 4.2% to 24,000 GWh from 22,989 GWh. This resulted from higher deliveries to residential (+5.8%), Commercial (+5.2%), Industrial (+6.3%), Governmental/Other (+0.1%), and was partly offset by a decrease in Wholesale (-8.4%).

Power Generation reported operating income of \$608 million vs. \$665 million as operating revenues rose to \$2.02 billion from \$1.93 billion and operating expenses increased to \$1.42 billion from \$1.27 billion. Operating expenses' increase came from higher electric fuel/other energy related purchases (+\$107 million), purchase electricity (+\$21 million), other operations/maintenance (+\$15 million), DD&A (+\$4 million), while other taxes were flat. Adjusted EBITDA declined to \$820 million from \$865 million and Power Generations contribution to D's overall earnings rose to \$0.63/share from \$0.57/share.

Total merchant generation sales to the NEPOOL Merchant fleet decreased 1.3% to 4,899 GWh from 4,962 GWh and PJM Merchant Fleet sales increased 5.4% to 2,115 GWh from 2,044 GWh.

Gas Infrastructure reported operating income of \$343 million vs. \$246 million. This occurred as operating revenues improved to \$843 million from \$663 million and despite operating expenses increasing to \$500 million from \$417 million. Operating expenses rose due to higher electric fuel/other energy-related purchases (\$29 million vs. \$4 million), other operations/maintenance (\$229 million vs. \$194 million), DD&A (\$160 million vs. \$134 million), and other taxes (\$77 million vs. \$62 million). These were partly offset by lower purchased gas expense (\$5 million vs.



\$23 million). Adjusted EBITDA improved to \$598 million from \$471 million and Gas Infrastructure's contribution to D's overall earnings increased to \$0.40/share from \$0.29/share.

Regulated Gas revenues declined to \$89 million from \$96 million and revenues from Regulated Gas Transmission/Storage fell to \$138 million from \$142 million. Natural gas deliveries increased to 162,507 mmcf from 152,544 mmcf.

D has a majority ownership in Dominion Midstream Partners (DM-\$18.25). During 3Q18 DM produced adjusted EBITDA of \$76 million and distributable cash flow of \$50 million. D's Board of Directors recently announced an offer to exchange each outstanding share of DM for a 0.2468 share of D. Management expects a definitive agreement to be produced during 4Q18 and with a closing during early 2019.

RECENT DEVELOPMENTS

The Atlantic Coast Pipeline (ACP) federal water quality permit, issued by the Army Corps of Engineers, was stayed by a US Appeals court. The permit involved the pipeline's water crossings in WV. The ACP is jointly owned by D, Duke Energy (DUK-\$85.29), and Southern Co (SO-\$47.40).

The ACP received issue permits from the VA Department of Environmental Quality to move forward with the pipeline in VA. FERC is expected to grant additional approval over the near term.

FuelCell Energy (FCEL-\$0.88) agreed to buy D's Bridgeport CT 14.9 MW fuel cell park.

D announced it was selling its 50% interest in the Blue Racer Midstream business for \$1.5 billion to First Reserve and affiliated investment funds.

A request was made by D for proposals to expand, by up to 500 MW, its planned solar and onshore wind power projects seeking to develop 3K MW of additional solar/wind power under the Grid Transformation & Security Act of Virginia.

D's CFO, Mark McGettrick, will retire on 1/1/19, and is being succeeded by Jim Chapman, effective 11/1/18. Chapman has been with D since 2013.

3 power plants were sold by D for \$1.32 billion in two separate transactions. The company sold its Fairless Power Station (1.240 MW combined-cycle gas turbine in PA), Manchester Street Power Station (468 MW combined-gas turbine in RI), and D's 25% interest in the Catalyst Old River Hydroelectric (192 MW hydro plant in LA).



A US Appeals Court ruled D did not violate the Clean Water Act after discharging arsenic from a VA coal ash storage site through groundwater into surrounding waters. This reversed a lower court ruling against D. The company estimates the cost to clean up its coal ash areas will cost approximately \$5.7 billion.

SCANA/D MERGER UPDATE:

D offered a new customer payout plan in order to continue its quest to acquire SCANA Corp. (SCG-\$41.30). The company proposed to extend the customer payback period to 20 years (from 8 years) and raise customer refunds to \$1.9 billion from \$1.3 billion. As part of the revised offer, D proposed to cut utility rates by ~\$20/month to SCG customers, from a previous offer of ~\$10/month, and accept a smaller profit from SCG's Summer nuclear project. Meanwhile, the US Nuclear Regulatory Commission approved the transfer of the VC Summer Nuclear power station in SC from SCG to D.

Our Thoughts

D reported 3Q18 operating earnings of \$1.15/share vs. \$1.04/share during 3Q17. The improvement was due to favorable weather in the regulated electric service territory, commercial operation of the Cove Point Liquefaction plant, and the positive impact of tax reform. These were partly offset by lower renewable energy investment tax credits and higher outstanding shares. While earnings were good there were two interesting developments during the quarter.

First, the SCG/D merger continues negotiations continue after D company proposed to extend the customer payback period to 20 years (from 8 years) and raise customer refunds to \$1.9 billion from \$1.3 billion. This new deal would not include the \$1,000 per customer refund previously proposed and the \$1.3 billion in refunds would instead be used to reduce SCG's nuclear debt. Politically, the proposal received "kudos" after the Speaker of SC's House said he supported the proposal. While this is a positive step, there is no guarantee the deal will be finalized.

Second, D is selling non-regulated assets and using the proceeds to pay down debt at the parent level. Proceeds from the \$1.5 billion sale of the company's ownership in the Blue Racer Midstream venture should close by year end and is part of management's overall plan to reduce its debt level by approximately \$8 billion. This should strengthen D's balance sheet over the near term.

We continue to rate D a HOLD since it is trading at 17.8x our 2018 earnings estimate. However, current shareholders should benefit from a current dividend yield of 4.5% with prospects of dividend increases going forward, assuming D increases profits during the next few years.



Risks

There is no guarantee D 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/regulatory rulings, tax issues, or rising operating costs could negatively impact D's earnings. D'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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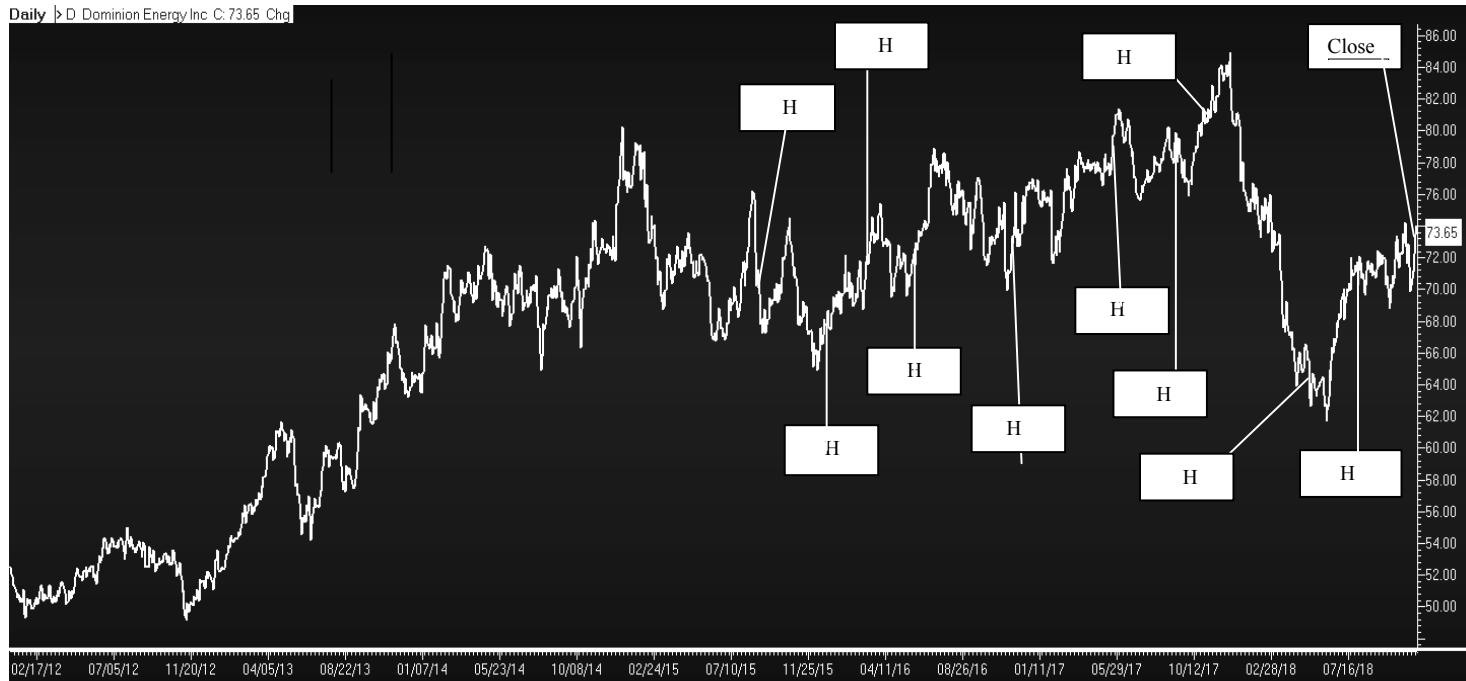


EQUITY RESEARCH

Dominion Resources (in millions, except per share data)										
	1Q17	2Q17	3Q17	4Q17	2017	1Q18	2Q18	3Q18	4Q18e	2018e
Operating Revenue	\$3,384	\$2,813	\$3,179	\$3,210	\$12,586	\$3,466	\$3,088	\$3,451	\$3,286	\$13,291
Operating Expenses										
Electric fuel/other energy-related purchases	575	498	638	590	2,301	744	623	761	594	2,722
Purchased electric capacity	-17	-12	21	14	6	14	23	50	28	115
Purchased gas	305	112	24	260	701	340	64	5	243	652
Other operations & maintenance	738	779	649	709	2,875	796	1,007	782	716	3,301
Depreciation, depletion, & amortization	469	467	485	484	2,905	498	463	526	477	1,964
Other taxes	189	168	162	149	668	199	166	177	156	698
Total operating expenses	2,259	2,012	1,979	2,206	8,456	2,591	2,346	2,301	2,214	9,452
Income from operations	1,125	801	1,200	1,004	4,130	875	742	1,150	1,072	3,839
Other income	116	60	73	-84	165	100	185	373	82	740
Income before interest & income taxes	1,241	861	1,273	920	4,295	975	927	1,523	1,154	4,579
Interest & related charges	292	308	305	300	1,205	314	361	378	319	1,372
Income before income taxes	949	553	968	620	3,090	661	566	1,145	835	3,207
Income taxes	275	136	272	713	30	135	88	262	175	660
noncontrolling interests	42	27	31	21	121	23	29	29	24	105
Reported Earnings	\$632	\$421	\$665	\$585	\$2,999	\$503	\$449	\$854	\$636	\$2,442
Reported Earnings Per Share	\$1.01	\$0.67	\$1.04	\$0.91	\$4.72	\$0.77	\$0.69	\$1.30	\$0.97	\$3.73
Items excluded from operating earnings (net of taxes)	\$21	\$31	\$7	\$727	\$709	\$238	\$111	\$96	\$25	\$470
Operating Net Income	\$611	\$390	\$658	\$1,312	\$2,290	\$741	\$560	\$758	\$651	\$2,710
Operating Earnings Per Share-Diluted	\$0.97	\$0.67	\$1.04	\$0.91	\$3.59	\$1.14	\$0.86	\$1.15	\$1.00	\$4.15

Important Disclosures

Daily > D Dominion Energy Inc. C: 73.65 Chg



11/27/09 \$36.14 Initiate BUY
6/18/10 \$42 Lower Rating to HOLD
Ratings:
Buy: B
Hold: H
Sell: S

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Steven Marascia owns shares of Dominion Energy

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