



April 20, 2018

**CURRENT PRICE:** \$77.68  
**RATING:** BUY  
**PRICE TARGET:** \$88  
**CURRENT YIELD:** 4.6%

**EPS Estimates**

	DEC 17A	DEC 18E
1Q	\$1.04	\$1.09
2Q	\$1.01	\$1.02
3Q	\$1.59	\$1.61
4Q	\$0.94	\$0.95
	<b>\$4.57</b>	<b>\$4.67</b>

**Trading Data**

52-WEEK PRICE RANGE: **\$91.80 - \$72.93**  
SHARES OUTSTANDING: **700(M)**  
MARKET CAP: **\$54,376(M)**  
AVG. DAILY TRADING VOLUME: **4.1(M)**  
S&P 500: **2,670**

**Valuation Data**

BOOK VALUE: **\$59.62**  
PRICE TO BOOK: **1.30x**  
DIVIDEND: **\$3.56**

**Duke Energy (NYSE: DUK)**

*Forward into 2018*

**Highlights**

- Adjusted diluted 4Q17 earnings of \$0.94/share vs. \$0.81/share
- Segment Income improved at all three operating units
- Results helped by weather & new US tax laws
- Unveils 2018 adjusted eps guidance to \$4.55-\$4.85/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%-4% 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 4.6% dividend yield, has both dividend and 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 four business units; Electric Utilities/Infrastructure, Gas Utilities/Infrastructure, Commercial Renewables, and Other. DUK provides electricity and natural gas to its customers, serving approximately 7.2 million electric customers in NC, SC, FL, IN, OH, and KY. DUK operates 150,900 miles of electric distribution lines and a 20,900-mile transmission system. The company has approximately 58,345 megawatts (MW) of electrical generating capacity with its plants fueled by coal, oil, natural gas, hydroelectric, renewables, and nuclear. DUK with Progress Energy in 2014 creating one of the largest electric utilities in the US and recently acquired Piedmont Natural Gas.

*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.*



# EQUITY RESEARCH

## Recent Earnings

DUK reported 4Q17 diluted earnings of \$1.00/share vs. (\$0.33)/share during 4Q16. The loss during 4Q16 was mainly the result of the loss incurred on the sale of DUK's International Energy unit. 4Q17's results were helped by colder weather during the quarter and from the positive effects of the new US tax laws. During 4Q17 DUK experienced improved operating results in its Electric Utilities/Infrastructure, Gas Utility/Infrastructure, and Commercial Renewables units, as all three saw increases in segment income. 4Q17 adjusted diluted earnings improved to \$0.94/share from \$0.81/share during 4Q16. DUK's FY17 diluted earnings improved to \$4.36/share from \$3.11/share during FY16 and adjusted earnings declined to \$4.57/share from \$4.69/share, when comparing the two periods.

## SEGMENT RESULTS

**ELECTRIC UTILITIES/INFRASTRUCTURE:** 4Q17's segment income rose to \$826 million from \$483 million during 4Q16. The improvement came from a \$231 million tax benefit resulting from the new Tax Act, favorable weather (+\$0.08/share), and lower operating/maintenance expenses (+\$0.11/share). This unit's operating revenues increased to \$5.10 billion from \$4.94 billion and operating expenses climbed to \$3.96 billion from \$3.95 billion.

Total electric sales improved 5.5% to 61,553 GWh from 58,345 GWh. The increase occurred in Wholesale/Other (+16.9%), Residential (+2.8%) and unbilled sales (+464%) and were partly offset by decreases in General Services (-0.9%), Industrial (-1.0%), and Other Energy Sales (-3.5%).

**GAS UTILITY/INFRASTRUCTURE:** This unit's segment income increased to \$140 million during 4Q17 from \$89 million during 4Q16. The increase came from a \$26 million tax benefit, customer growth, and higher integrity management investments at the Piedmont Gas subsidiary (+\$0.02)/share, and improved earnings from the Atlantic Coast Pipeline investment (+\$0.01/share). Total sales from Piedmont Natural gas rose 10.4% and Duke Energy Midwest improved 12.7%.

**COMMERCIAL RENEWABLES:** Segment income improved to \$439 million during 4Q17 from \$10 million during 4Q16. The improvement was the result of a \$442 million tax benefit (New Tax Act), a new wind project brought online in late 2016, and improved wind resources. Factoring the positive tax impact, on an adjusted basis, segment income was \$15 million vs. \$10 million. When comparing the two quarters, renewable plant production rose 8.7% to 1,984 GWh from 1,825 GWh.



OTHER: This unit includes corporate interest expense not allocated to DUK's business units, results from DUK's captive insurance company, and other investments including National Methanol Company (an equity method investment). Expenses during 4Q17 increased to \$700 million from \$209 million during 4Q16. The increase was the result of a \$597 million New Tax Act charge and higher income tax expense (-\$0.05/share).

## RECENT DEVELOPMENTS

DUK and Hawaii Electric (HE-\$34.30) began construction of 20 MW solar project at the US Navy's Joint Base Pearl Harbor-Hickam West Lock Annex.

DUK agreed to pay a \$156,000 fine for polluting ground and surface waters with coal-ash waste around three power plants in NC. According to the NC Department of Environmental Quality, there are still 8 additional plants which need to be inspected to determine if additional penalties are warranted against DUK.

The company announced it would invest \$1.1 billion in natural gas, solar, and wind power generation by 2026 and another \$25 billion in smart electric grid technologies, as well as putting electric lines underground. DUK's goal for 2030 is to have 10% of its electricity come from renewable sources, 16% from coal, 32% from nuclear power, and 42% from natural gas.

FERC decided to delay its ruling on the State of NY's decision to deny a key water permit for the Constitution Pipeline owned by DUK, Williams Co. (WMB-\$25.51), Cabot Oil & Gas (COG-\$23.08), and WGL Holdings (WGL-\$85.33). This freezes the NY State denial of the water permit until FERC decides on the next step in this regulatory process.

DUK management stated the new tax law, recently passed by the US Congress, could reduce 2018 earnings growth by 2%, or equate to approximately \$0.13/share, due to the reduction of the value of existing tax benefits of financing at the corporate level as the tax rate fell from 36% to 21%.

DUK is seeking storm cost recovery from the Public Service Commission of Florida following the damage caused by Hurricane Irma. The request is to be reimbursed for approximately \$381 million in costs caused by the hurricane.



# EQUITY RESEARCH

## Our Thoughts

DUK reported 4Q17 diluted earnings of \$1.00/share vs. (\$0.33)/share during 4Q16 and 4Q17 adjusted diluted earnings improved to \$0.94/share from \$0.81/share during 4Q16. While there was operational improvement in DUK's operating units, a large part of the gain came from the tax benefits created by the new tax laws recently passed by the US Congress.

The lower tax rates, however, will probably cause DUK, and all US utilities, to lower customer rates in accordance with most state's utility regulations. Despite this scenario, DUK management believes it will still be able to grow its forward earnings. Earlier guidance, prior to the recent tax cut, was a 4%-6% annual growth rate through 2020 and allowed for dividend increases going forward. Now, DUK believes the growth rate is likely to be in the lower end of the 4%-6% range during 2018 and could accelerate to the higher end of the range during 2019 and beyond. Additionally, DUK unveiled 2018 earnings guidance of \$4.55-\$4.85/share.

We continue to rate DUK a BUY for income/growth investors. These shares currently pay a dividend yield of 4.9%, with the potential of rising dividends, as earnings continue to grow during the next few years. The increase of both dividends and earnings could allow DUK's shares to appreciate in price. Our price target is \$88/share, equating to 1.48x its book value of \$59.62/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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# EQUITY RESEARCH

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

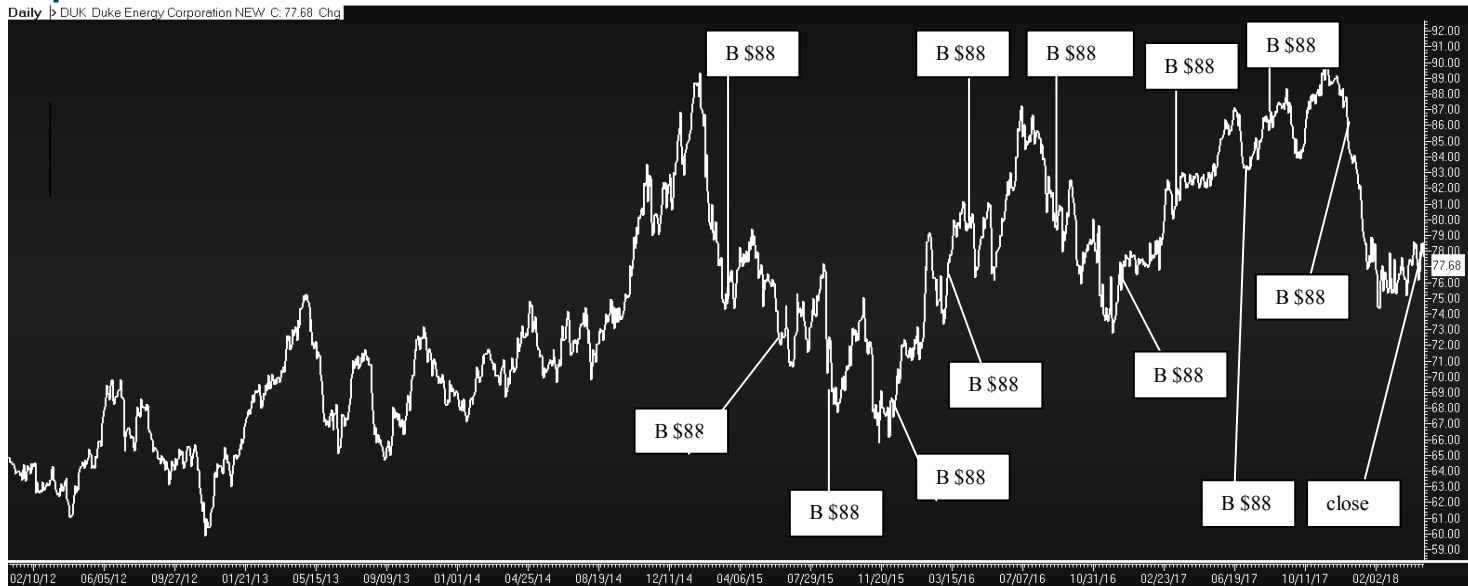
	1Q17	2Q17	3Q17	4Q17	2017	1Q18e	2Q18e	3Q18e	4Q18e	2018e
<b>Operating Revenues:</b>										
Regulated electric	\$4,913	\$5,118	\$6,091	\$4,995	\$21,777	\$4,867	\$5,019	\$6,041	4,923	\$20,850
Non-regulated electric/natgas/other	646	162	144	782	1,734	654	226	195	718	1,793
Regulated natural gas	170	275	247	32	654	181	283	209	94	767
Total Operating revenues	5,729	5,555	6,482	5,799	23,565	5,702	5,528	6,445	5,735	23,410
<b>Operating Expenses:</b>										
Fuel electric gen. & purchased power-reg	1,449	1,541	1,863	1,497	6,350	1,486	1,528	1,917	1,476	6,407
Cost of natural gas & coal sold	258	76	66	232	632	243	104	129	279	755
Operation, maintenance, & other	1,433	1,407	1,442	1,504	5,788	1,487	1,459	1,491	1,554	5,991
Depreciation & Amortization	859	835	900	1,023	3,527	981	878	926	933	3,718
Property & other taxes	304	307	313	309	1,233	307	311	314	317	1,249
Impairment charges		9	207	66	282					
Total Operating expenses	4,303	4,175	4,793	4,550	17,812	4,504	4,280	4,777	4,659	18,220
Gains/losses sale of other assets (net)	11	7	6	4	28	5	9	6	7	27
Operating Income	1,437	1,387	1,695	812	5,781	1,203	1,257	1,674	1,083	5,217
<b>Other Income/Expenses</b>										
Equity in earnings of unconsolidated affiliates	29	36	36	18	119	22	27	33	37	119
Impairments/Gains on unconsol affiliates sales										
Other Income/Expenses	86	81	88	97	352	85	83	81	94	343
Total other income/expenses	118	117	124	112	471	107	110	114	131	462
<b>Interest expense</b>	491	486	498	511	1,986	512	519	524	526	2,081
Income from Cont Ops before Income Taxes	1,081	1,018	1,321	846	4,266	796	848	1,264	688	3,596
Income tax expense	344	327	364	161	1,196	175	187	276	144	782
Income from Cont Operations	717	691	957	705	3,070	621	661	988	544	2,814
Income (loss) from Discontinued Ops		-2	-2	-2	-6	-2	-2	-3	-1	-8
<b>Net Income</b>	717	689	955	703	3,064	619	659	985	543	2,806
Net Income/loss attributable to non-controlling interest	-1	-3	-1		-5	-3	-1	-2	-1	-7
Net Income attributable to Duke Energy Corp	\$716	\$686	\$954	\$703	\$3,059	\$616	\$658	\$983	\$542	\$2,799
<b>Diluted EPS</b>	\$1.02	\$0.98	\$1.36	\$1.00	\$4.36	\$0.88	\$0.94	\$1.40	\$0.77	\$3.99
Net Income from discon ops attributable shareholders										
Diluted EPS	\$1.02	\$0.98	\$1.36	\$1.00	\$4.36	\$0.88	\$0.94	\$1.40	\$0.77	\$3.99
Adjustments	\$0.02	\$0.03	\$0.23	\$0.06	\$0.21	\$0.21	\$0.08	\$0.21	\$0.18	\$0.68
Adjusted Diluted EPS	\$1.04	\$1.01	\$1.59	\$0.94	\$4.57	\$1.09	\$1.02	\$1.61	\$0.95	\$4.67



# EQUITY RESEARCH

## Important Disclosures

Daily | DUK Duke Energy Corporation NEW C: 77.68 Chg



- 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 1.48x book value/share

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Analyst owns/controls family account containing shares of Duke Energy

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