REFINITIV STREETEVENTS

EDITED TRANSCRIPT

EVRG.N - Q3 2022 Evergy Inc Earnings Call

EVENT DATE/TIME: NOVEMBER 04, 2022 / 1:00PM GMT

REFINITIV

CORPORATE PARTICIPANTS

David A. Campbell *Evergy, Inc. - President, CEO & Director*

Kirkland B. Andrews *Evergy, Inc. - Executive VP & CFO*

Lori A. Wright *Evergy, Inc. - VP of IR & Treasurer*

CONFERENCE CALL PARTICIPANTS

Dariusz Lozny *BofA Securities, Research Division - Research Analyst*

PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the Third Quarter 2022 Evergy Earnings Conference Call. (Operator Instructions). Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Lori Wright, Vice President of Investor Relations and Treasurer. Please go ahead.

Lori A. Wright - *Evergy, Inc. - VP of IR & Treasurer*

Thank you, [Alyssa]. Good morning, everyone, and welcome to Evergy's third quarter call. Thank you for joining us this morning.

Today's discussion will include forward-looking information. Slide 2 and the disclosure in our SEC filings contain a list of some of the factors that could cause future results to differ materially from our expectations and include additional information on non-GAAP financial measures. The releases issued this morning, along with today's webcast slides and supplemental financial information for the quarter, are available on the main page of our website at investors.evergy.com.

On the call today, we have David Campbell, Evergy's President and Chief Executive Officer; and Kirk Andrews, Executive Vice President and Chief Financial Officer. David will cover our third quarter highlights, provide an update on ongoing and upcoming regulatory proceedings and our recent sales trends, as well as an update on our resource planning and the Inflation Reduction Act. Kirk will cover in more detail the third quarter and year-to-date results and our financial outlook for the remainder of the year. Other members of management are with us and will be available during the question-and-answer portion of the call.

I will now turn the call over to David.

David A. Campbell - *Evergy, Inc. - President, CEO & Director*

Thanks, Lori, and good morning, everyone.

I'll begin on Slide 5, and I'm pleased to report that we had another solid quarter as we delivered adjusted earnings of $2.01 per share compared to $1.97 per share in 2021. The increase in adjusted earnings over last year was driven primarily by favorable demand, above normal weather and higher transmission margin, partially offset by higher D&A and interest expense. For year-to-date, September 30, adjusted earnings were $3.43 per share compared to $3.35 per share a year ago.

With these strong results, we are raising the midpoint of our guidance from $3.53 per share to $3.58 per share, and revising our adjusted EPS guidance range to $3.53 to $3.63 per share from $3.43 to $3.63 per share. Kirk will detail the drivers of our third quarter performance and upward guidance revision.

I would also like to call out and complement the strong work of the entire Evergy team in providing safe and reliable power to our customers and communities through a hot summer and early fall. In particular, I'll call out our team's strong safety performance with a 66% reduction in DART events and a 62% reduction and OSHA recordables compared to the first 9 months of 2021.

On August 9, we announced an agreement to acquire Persimmon Creek Wind Farm, a 199-megawatt operating wind farm in Western Oklahoma, for $250 million. This investment satisfies 2/3 of our planned 300 megawatts of renewal additions in 2024. Persimmon Creek will deliver low-cost power to our Missouri West customers, subject to approval from the Missouri Public Service Commission, and supports our carbon reduction and net zero emission targets.

We also announced a 7% increase in our quarterly dividend to $0.6125 per share or $2.45 per share on an annualized basis. This increase is consistent with our recent growth trajectory and long-term targets. We remain laser-focused on executing our plan and advancing our strategic objectives of affordability, reliability and sustainability in the context of historically volatile economic conditions and inflation. We remain confident in our long-term plan, and we are reaffirming our target annual EPS growth rate of 6% to 8% from 2021 to 2025.

Now moving to Slide 6 in Missouri, we are pleased to reach partial stipulations and agreements with our stakeholders in the pending Metro and Missouri West rate cases, which we expect will provide a balanced outcome for customers and shareholders. The approved agreements call for a $67.5 million revenue increase across our Missouri jurisdictions. Not all of the relevant details are public in the Black-box settlement, but I'll highlight the 8.25% pre-tax rate of return for plant and service accounting, or PISA, as a helpful data point. This will apply to go-forward investments. While the settlement resolved most of the key economic issues, there are several items that the Missouri Commission will resolve in the coming weeks. Revised rates will go into effect on December 6.

We're pleased that we were able to find common ground with our stakeholders in these settlements. We continue to view Missouri as a very attractive jurisdiction to invest in, as evidenced by the rate case and the constructive extension and changes to the PISA legislation that were enacted earlier this year.

Turning to Slide 7, I'll provide a summary of other key regulatory and legislative milestones and ongoing constructive developments in both Kansas and Missouri.

I'm happy to report the Missouri Commission issued a financing order in October that approved our request to recover and securitize approximately $300 million of Winter Storm Uri costs at our Missouri West jurisdiction. We expect to go to market in the first half of 2023 to complete this financing.

For the Persimmon Creek acquisition, we filed for a Certificate of Convenience and Necessity, or CCN, in August. We expect this investment to qualify for PISA treatment at our Missouri West jurisdiction. Missouri Commission staff will issue its recommendation by November 18, and we requested approval by year-end.

On the other side of the state line, the Kansas Corporation Commission issued an order in mid-September that determined our 2022 capital investment plan meets the requirements of the capital investment plan framework. Consistent with prior years, the commission also requested Evergy attend a workshop to explain the impact of the proposed capital spending and to answer questions for the commissioners, KCC staff and the Citizens' Utility Ratepayer Board or CURB. The workshop will take place on December 13.

We look forward to the opportunity to highlight the benefits of our planned transmission and distribution investments in a system with a lot of older infrastructure, the addition of renewables consistent with our integrated resource plan, the benefits of which are now further enhanced by the federal subsidies in the IRA, as well as upgrades to technology and customer service platforms that will help us to serve customers more effectively and efficiently. In addition, we'll cover our ongoing progress in advancing the regional rate competitiveness of Evergy's system, which is a core element of our strategic focus on affordability.

Also in Kansas, preparation is underway for our 2023 rate cases, which we will file in late April. This will be our first request for new base rates in Kansas since we formed Evergy in 2018. Key drivers of the case will include return on equity, capital structure, review of our reliability and efficiency-focused distribution, customer and technology infrastructure investments since our last rate case, as well as passing on the significant O&M savings we've generated for customers since the completion of the merger.

We look forward to working constructively with our regulators and stakeholders just as we have in multiple forms of the past few years in campus, to advance the 2023 rate cases and deliver against our strategic objectives of ensuring affordability, reliability and sustainability for our Kansas customers and communities.

Turning to Slide 8. I'll review our demand growth and comment on economic trends and developments. For the third quarter, total weather-normalized retail demand increased by approximately 1.7%, driven by a robust increase in industrial demand for the chemical and oil and gas sectors. Year-to-date, weather-normalized demand is up approximately 2%. Total demand is up 2.4% for the quarter and approximately 3% for the year. While 2021 was warmer than average, temperatures were even higher than the third quarter of 2022.

Our regional economy has remained healthy as the unemployment rate in both Kansas and Missouri continues to track below the national average. We are also excited by the ongoing growth that we've seen as reflected in the numbers I just shared, as well as the large project announcements such as Meta's Data Center and Panasonic's new electric vehicle battery manufacturing plant.

I'll conclude my remarks with a few comments on the Inflation Reduction Act, or IRA, on Slide 9. There's no question that the IRA is a very consequential piece of legislation. We are assessing the key impacts of the IRA through the economic and customer affordability lenses as the bill provides longer-term certainty and visibility for significant renewable energy tax credits and emerging technologies. This economic support will further enhance our ability to take advantage of the abundant renewable potential of our region and deliver savings to our customers by replacing energy produced from resources with higher fuel and O&M costs. We also expect the Wolf Creek nuclear plant to be eligible for the IRA's nuclear production tax credit, which will have a beneficial impact for customer bills in years with low realized prices for Wolf Creek.

We expect to provide an update on our future renewable generation plans by mid-2023 when we file our revised annual integrated resource plans in Kansas and Missouri. This update will incorporate the impact of the IRA, updated commodity projections and higher capacity requirements in the Southwest Power Pool. We are excited to advance the program that will further enhance our affordability, reliability and sustainability goals.

I will now turn the call over to Kirk.

Kirkland B. Andrews - *Evergy, Inc. - Executive VP & CFO*

Thanks, David, and good morning, everyone.

I'll start with the results for the quarter on Slide 11. But before I turn to the drivers behind our third quarter adjusted EPS, I'd like to summarize one item on our GAAP results for the quarter related to the deferral of certain revenues from our retired Sibley coal plant in Missouri.

Although rate treatment for Sibley is among the items the Missouri Public Service Commission will resolve in the coming weeks, a decision by the commission issued in August related to a plant retirement by another Missouri utility established a regulatory precedent, which led us to change the accounting for Sibley. Since retiring Sibley in 2018, we've collected approximately $3.1 million in revenues each quarter associated with the return on the Sibley rate base. Based on the regulatory precedent in the third quarter, we deferred the cumulative amount of these revenues collected in rates since the plant retirement, totaling $47.5 million, to a regulatory liability with a corresponding reduction to operating revenues in the quarter.

In order to allow our adjusted EPS to reflect the impact of the accounting change in the periods in which revenues were collected, we've excluded the amount of the deferral associated with the revenues collected prior to the third quarter and prior to 2022 from our third quarter and year-to-date adjusted EPS, respectively. As a result, within the quarter and year-to-date, the net impact of the change in Sibley accounting reflected in our adjusted EPS was approximately $0.01 for the quarter and $0.03 year-to-date. For comparative purposes, we've also recast the adjusted EPS for 2021 to reflect the $0.01 per quarter impact.

Notwithstanding this change in accounting, we remain confident that the retirement of Sibley was prudent as reflected in the Commission Order in the Missouri West securitization proceeding, which addressed prudence. As such, we continue to believe the inclusion of ongoing return on rate base per Sibley in our general rate case filing was appropriate. Although the ultimate rate treatment of Sibley, including the ongoing return on rate base, remains to be decided upon by commission, and this decision may have an impact on future revenues.

The third quarter deferral of revenues in and of itself does not impact our expected earnings going forward. For the third quarter of 2022, Evergy delivered adjusted earnings of $462 million or $2.01 per share compared to $452 million or $1.97 per share in the third quarter of 2021.

The year-over-year increase in third quarter EPS was driven by the following. First, a 3% increase in cooling degree days drove a $0.03 increase in EPS compared to third quarter '21. Adjusting for the warmer-than-normal weather experienced in the third quarter of '21, however, the third quarter of this year also saw $0.15 of EPS versus normal weather assumed in our original plan. As David mentioned earlier, we also saw a 1.7% increase in weather-normalized demand this past quarter, which drove $0.06 per share. Higher transmission revenues resulting from our ongoing investments to enhance our transmission infrastructure and higher volumes drove about a $0.01 increase.

These positive drivers were partially offset during the quarter by higher operation and maintenance expense as well as increased depreciation expense, which impacted our EPS by $0.01 and $0.03 per share, respectively. Additionally, we have incurred $0.03 of higher interest expense due to increased debt outstanding at higher rates.

I'll turn next to year-to-date results, which you'll find on Slide 12. For the 9 months ended September 30, adjusted earnings were $790 million or $3.43 per share compared to $768 million or $3.35 per share for the same period last year.

Again, moving from left to right, our year-to-date EPS drivers versus '21 include the following. When combined with above normal weather in the first 2 quarters, our year-to-date results now reflect a $0.09 benefit from weather versus last year. When compared to normal weather, weather this year contributed $0.26 year-to-date. Weather-normalized demand increased about 2% year-to-date, driving approximately $0.15 of EPS. Higher transmission revenues driven by ongoing investments, combined with an increase in transmission delivery charge revenues due to higher volumes, led to $0.12 year-to-date increase versus '21.

And these items were partially offset by increased O&M expense due to higher generation maintenance driven by weather and outages as well as increased vegetation management, leading to approximately $0.07 per share. $0.08 of higher depreciation expense due to increased infrastructure investment, $0.05 of increased interest expense and lower AFUDC equity, again, primarily driven by higher debt outstanding at higher interest rates. $0.02 of income tax smoothing driven by timing differences within the year. And finally, we had $0.06 of other items, primarily from lower COLI proceeds and higher property taxes incurred prior to the implementation of the new Missouri property tax tracker in late August.

Turning to Slide 13, I'll provide greater details on the drivers of our increased midpoint and narrowed guidance range for 2022. Starting with our previous guidance range on the left of the slide, and again, moving from left to right.

First, we incorporate the $0.26 of weather impact year-to-date, assuming normal weather for the fourth quarter. Higher transmission revenues driven by an increase in TDC revenues due to higher volumes drives a $0.09 increase versus original expectations. These items are partially offset by an $0.11 per share increase in O&M driven by increased generation maintenance to maximize fleet availability due to higher-than-expected demand and power prices year-to-date and higher vegetation management spend. $0.09 per share from COLI driven by immaterial COLI proceeds year-to-date and assuming no further COLI proceeds in the fourth quarter. $0.06 driven primarily by higher interest expense. And lastly, we've incorporated the $0.01 per quarter impact of the Sibley deferral or $0.04 for the year into our updated guidance.

And finally, turning to Slide 14, having raised our midpoint guidance for 2022 and increased our dividend by $0.07 to $2.45 per share annualized, we are reaffirming our 2021 to 2025 long-term annualized EPS growth target of 6% to 8% and continue to target dividend growth in line with EPS at a 60% to 70% payout. We'll be providing 2023 adjusted EPS guidance on our fourth quarter call in February, and we'll be filing our Kansas rate case in late April of next year, with rates effective in late December. We continue to plan $10.7 billion of infrastructure investments from 2022 to 2026, and we'll provide an update to our CapEx plan on our fourth quarter call as we maintain focus on making investments to ensure we provide affordable, reliable and sustainable service to our customers and communities.

With that, operator, we'd be happy to take questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of [Angelique] (inaudible) with Bank of America.

Dariusz Lozny - *BofA Securities, Research Division - Research Analyst*

This is Dariusz on for Julien.

First one is I just wanted to maybe check in on status or progress thus far on wind PPA buy-ins? I think earlier in the year, you guys expected to do at least one of those. Just curious if you could give an update or maybe any kind of updated expectations as that process moves along?

David A. Campbell - *Evergy, Inc. - President, CEO & Director*

Sure. I'll hand that over to Kirk. This is David, and appreciate the question, Dariusz.

As you would expect, the evolution of the Inflation Reduction Act and the -- created some uncertainty in the market puts around what the substitute would be and whether they would occur, and that has created some dynamics with respect to both considering what valuation is and what the future potential could be. And we now have clarity around that, of course, but folks are still settling on respective values. We think that on balance, it further enhances the value proposition where we're proposing in terms of the benefits to potential sellers and for us, the potential buyers and what we can offer to customers. But it has impacted time if you agree, but I'll hand it over to Kirk who's driving that process.

Kirkland B. Andrews - *Evergy, Inc. - Executive VP & CFO*

Sure. I'll just add to that we haven't changed that objective, and we're still focused on getting at least one of those done. We're still in active dialogue with counterparties on that front. Can't absolutely predict the timing. Obviously, we're within a couple of months of the year-end, but we are laser-focused on that objective. And if the time extends a little beyond the year-end, that doesn't change that focus on at least getting one of those done. And that, again, is incremental to our plan, both from a capital and EPS perspective.

David A. Campbell - *Evergy, Inc. - President, CEO & Director*

And we've been pleased with -- Kirk and his team were able to negotiate and agree to the acquisition of Persimmon Creek. That's an operating wind farm. We hope to get approval on that by year-end, but -- and have that in the -- certainly have that in the system next year. And as an operating wind farm that's added to our portfolio earlier than what was in our IRP that was just part of our 2024 plan.

Dariusz Lozny - *BofA Securities, Research Division - Research Analyst*

Okay, great.

And maybe just a follow-up on the Sibley change in accounting treatment. Can you maybe just discuss a little bit sort of like prospectively, what is included in forward guidance relative to that change in accounting treatment? And also how, I guess, the pending order from the PSC in Missouri can affect the range of outcomes there?

Kirkland B. Andrews - *Evergy, Inc. - Executive VP & CFO*

Sure, Dariusz. First of all, in terms of -- in our forward expectations, as you know and as I indicated, part of our rate filing in Missouri included the ongoing return on Sibley. That's something we've discussed before, so that is obviously pending in front of the commission, and that's in our expectations. We've kind of talked about the order of magnitude of what that means from an EPS perspective on a go forward, about $0.03.

Drawing the distinction between that and the accounting change however, as I indicated in my remarks, the deferral to the regulatory liability, although that does change in hindsight as well we've recast our adjusted EPS by that $0.01 a quarter. Looking forward, as I also indicated, that does not change our expected earnings on a go-forward basis. The accounting change does not change our expected earnings.

David A. Campbell - *Evergy, Inc. - President, CEO & Director*

Yes. So the Sibley item remains open. We'll expect the commission ruling -- really, it could be as soon as this week or in the coming weeks, certainly because our rates go in effect December 6. As Kirk described, it's about $0.03 of exposure going forward. And you may say, well, gosh, if it's $0.01 a quarter this year, why is it lower? It's because of the -- that's the amount that was set in rates in the last rate case. It's a lower balance. Going forward, that's under review.

And there are a couple of items that the Missouri Commission will review, and Sibley is one. We always expected that we get a lot of attention in the rate cases as it was a complicated situation. But we were pleased to get constructive settlement on the main issues in the rate case, and we'll have resolution on the remaining couple in the coming weeks.

Operator

That concludes today's question-and-answer session. I'd like to turn the call back to David Campbell for closing remarks.

David A. Campbell - *Evergy, Inc. - President, CEO & Director*

Well, that was efficient.

So I'll wrap up by starting with a special thanks to Lori Wright, who will be retiring from Evergy this year after 21 years with the company and its predecessors in nearly 4 decades in the industry. Lori, we greatly appreciate your outstanding service and contributions, and we know that (inaudible) has large shoes to fill.

For everyone on the call, we appreciate your time with us today, and have a great day.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.
