Wells Fargo - SCG: Constructive Settlement Reached On Fixed-Price Option

Summary. On 9/1, SCG announced a settlement agreement with a number of intervenors including the South Carolina Office of Regulatory Staff (ORS) related to the company’s election of the Fixed Price Option (FPO) for the new nuclear development (NND). Key provisions of the agreement include approval of an incremental $831mm of capital costs and a modest reduction of the allowed ROE for NND to 10.25% from 10.5% to be applied (essentially) to new NND capital spend incurred post 6/30/16. Bottom line – we view the agreement as constructive and supportive of our positive rating on SCG - particularly as it relates to our longstanding thesis that there exists strong stakeholder support for new nuclear in SC. No change to our 16E & 17E of $4.00 & $4.25. We are modestly increasing our 18E to $4.75 from $4.65 to reflect an accelerated NND capex recovery vs. our prior assumption (model revision). We reiterate our Outperform rating and 12-18 month valuation range of $78-80/share.

Next Steps. Since the settlement is not unanimous, there will be a public hearing on 10/4. That being said, the settlement includes a number of highly influential parties including the ORS and an industrial users group. The SC Public Service Commission (PSC) is scheduled to issue a final decision by 11/28. Based on historical precedent, we would be surprised if the final order included any material modifications to the settlement. Along with the approved incremental capital costs and 10.25% ROE, other elements of the settlement include an approval of the updated schedule, which contemplates substantial completion dates of August 2019 (Unit 2) and August 2020 (Unit 3) and, separately, an agreement on the part of SCG to not request approval of any additional costs prior to 1/28/19.

EPS Outlook. Our 16-20E EPS are $4.00, $4.25, $4.75, $4.90 & $5.15, which results in a 6-7% CAGR off the 2015 weather-normalized base of $3.73. Based on our calculations, the 25 bp reduction in the ROE for prospective NND capex only had a modest $0.01-0.03 negative impact on our 2018-20 EPS estimates. Our outlook assumes additional new equity of $550mm during 2017 & 2018.

Valuation Range: $78.00 to $80.00

Our $78-80/sh valuation range is based on a P/E multiple (apply a ~5% discount to the 17E Regulated Electric median of 17.5-18.0X to our 18E of $4.75) and DDM analyses. Risks include regulatory and construction.

Investment Thesis:
We view SCG’s ~10% P/E discount to be excessive as the above-average nuclear construction risk is partially offset by above-average EPS growth and a supportive regulatory environment, including timely BLRA recovery of new nuclear CapEx.

Mizuho - Da-Fix Means De-risk; Reiterate Buy; Remains a Top Pick
Event: SCGs flagship utility, South Carolina Electric & Gas, reached what we view to be a milestone settlement agreement related to its new nuclear build. Under the settlement, SCE&G will take a 25 basis point reduction in exchange for the ability to recover an additional $831 million in higher nuclear costs, and fix the contract price with its EPC vendor, Westinghouse Electric. Total project cost becomes approximately $7.7 billion. Importantly, the settlement supports the approval of the updated contract schedule which would have the two new units substantially completed by August 2019 and August 2020, meaning there are likely no additional delays. The key parties to the settlement include the S.C. Office of Regulatory Staff, key electric cooperatives, and the industrial user groups. Absent from the agreement are the Sierra Club, Coastal Carolina Conservation League, and CMC Steel. Upon first look, the settlement agreement mirrors exactly our expectations. As of this writing, SCG has not filed an 8-K with the complete settlement report.

Implication: The settlement agreement, if approved by the SC regulators, helps: (i) de-risk the story on many fronts but most importantly, by removing any variable price exposure SCE&G might have otherwise had with the nuclear build; (ii) reduce the discounted valuation; (iii) rebases its earnings growth profile; (iv) allows investors to concentrate on a likely acceleration in the dividend growth rate towards the end of the decade to return to a 60% payout ratio; and (v) allows investors to concentrate on how SCG will redeploy the roughly $550 million in annual cash flow from these two new nuclear units. Hearings on the proposed settlement are slated to begin **October 4, 2016**. We expect regulatory approval on or around mid-November.

Expected Stock Reaction: POSITIVE
Our 2016, 2017, 2018, and 2019 EPS estimates remain unchanged at $4.02, $4.15, $4.60, and $5.00, respectively, which already reflect the fixed price option. Our 2018 estimate is approximately $0.13 per share above current Street consensus (having inched up from $4.40/sh.) as more analysts include the fixed price option. Our 2018 EPS estimate reflects $500 million in secondary equity issuances in that year (using mid-year convention) to support the balance sheet as well as roughly $100-125 million in annual DRIP (consistent with management disclosure). SCG previously articulated 4-6% EPS growth exclusive of the fixed price deal; thus, we expect the current 9% discount on our 2018E EPS to begin to abate as earnings expectations are re-based higher.

UBS - Fixing a Deal on a Fixed Price Contract
SCG files settlement with interveners on fixed price nuclear deal
Mgmt successfully filed a settlement with ORS and a variety of other SC parties as part of its petition to increase rates to reflect principally the costs associated with implementing a fixed price deal for its VC Summer nuclear expansion. Hearings are still scheduled for **Oct 4** with a decision from the PSC expected in ~Nov. We see the project as substantially de-risked with this deal; we note the updated CWIP figures reflecting this higher spend were already introduced with 2Q. We look for an update by **Oct 1** on the final timing for Construction Milestone payments with Fluor, which could tweak CWIP on the project (hence EPS). The finalization of this schedule should allow for the SC PSC to have the final view on payments by the time it votes.

What are they giving up? No further capital cost increases pre '19
In turn, mgmt. commits to avoid further increases in capital costs pre **Jan 28, 2019**, just a few months before the scheduled Aug 2019 in-service date of Unit 2 (slight delay from last order of Jun 2019). We note the deal includes interveners with a contingency for project delay of 18-
months+ (presumably to line up with the end of ~2020). Experts we’ve spoken to believe efforts appear under way to provide for a potential PTC qualification extension beyond the 12/31/2020 deadline (potentially indefinitely).

**We remain concerned around future project delays**
We are wary re progress on the site as hiring activities by Fluor ramp and overall productivity appears above 1.0. We believe the project could still be readily delayed, but the question is whether any such delay would be beyond the end of 2020. We note the order only limits the company's ability to file for further increases until 2019, rather than preventing it from doing so. From an investor perspective the limited ability to file for the time being should substantially de-risk near-term EPS as the SCG will not seek deals beyond the scope defined. A deal was also reached in NC earlier this week.

**Also locking in new nuclear ROE at reduced rate of 10.25% through build**
Mgmt is also further reducing its ROE on the Summer project to 10.25% from 10.5% (already lowered from 11% from the last deal). Notably this is consistent with SCE&G's currently authorized ROE of 10.25% (to which it would have dropped once reaching inservice anyway). We are not surprised by this aspect of the deal; mgmt also used this lever in the last round of negotiations.

**We expect the shares to trade up on deal announcement.**
While not additive to 2Q disclosures on CWIP, we think the deal de-risks the shares. We note consensus remains conservative, with this latest deal allowing for positive estimate revisions (albeit offset in part by the slightly lower ROE). Ahead of final payment update on 10/1, we maintain our estimates at the top end of mgmt's 4-6% EPS growth rate; our estimates are somewhat conservative to reflect the risk of future execution slip.

**Barclays - SCG: Settlement Agreement for Fixed Price Option on New Nuclear**
On September 1, SCE&G announced that it had entered into a settlement agreement with the South Carolina Office of Regulatory Staff, the Central Electric Power Cooperative Inc., The Electric Cooperatives of South Carolina, Inc., Frank Knapp Jr., and South Carolina Energy Users Committee related to SCE&G's petition to update construction and capital cost schedules, including SCE&G's election of the Fixed Price Option for the two new nuclear units under construction. The settlement agreement is subject to approval by the Public Service Commission of South Carolina. A public hearing on SCE&G's petition is scheduled to begin October 4, 2016. The settlement agreement signifies that no contested issues exist among the settling parties and supports approval of the updated construction schedule. The settlement supports the inclusion of an additional $831M in the capital cost schedule. In addition to supporting the new schedule and increased cost, the settling parties agreed to revised the allowed ROE from 10.50% down to 10.25%. The new ROE will be applied prospectively for all costs recovery sought on or after January 1, 2017, until such time that the new nuclear units are completed. SCE&G also agreed not to file future requests to amend the capital cost schedule prior to January 28, 2019.

We find this a constructive settlement that if approved will move to further limit the risk associated with nuclear new build project. The 25bp reduction in ROE is in line to better than expectations given the settlement for the last major cost and schedule change resulted in a 50bp reduction in allowed ROE. We await a final order to determine the profile of the
additional $831M in capital costs along with any associated change in financing from debt and equity in support of the increased costs.

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September 1, 2016

Equity Research

SCANA Corporation

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Please see page 3 for rating definitions, important disclosures and required analyst certifications
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Headquartered in Cayce, South Carolina, SCANA's businesses include regulated electric and natural gas utility services, gas transmission and retail gas and energy marketing. The company's primary subsidiary, South Carolina Electric and Gas (SCE&G), serves 688,000 electric utility customers and 325,000 natural gas customers in central, southern, and southwestern portions of South Carolina. Public Service North Carolina serves 500,000 natural gas customers in north, central, Piedmont, and western parts of North Carolina. SCG is also involved in retail natural gas marketing in Georgia and wholesale energy marketing in the Southeast.
Required Disclosures

SCANA Corporation (SCG) 3-yr. Price Performance

Date | Published Price ($) | Rating Code | Val. Rng. Low | Val. Rng. High | Close Price ($) |
-----|---------------------|-------------|--------------|---------------|----------------|
8/27/2013 | NA | 1 | 58.00 | 59.00 | 48.46 |
8/30/2013 | 48.10 | 1 | 54.00 | 55.00 | 48.12 |
3/17/2014 | 50.99 | 1 | 59.00 | 60.00 | 50.59 |
4/24/2014 | 52.56 | 1 | 60.00 | 61.00 | 52.56 |
6/10/2014 | 53.65 | 1 | 53.00 | 54.00 | 53.81 |
8/1/2014 | 53.88 | 1 | 60.00 | 61.00 | 50.88 |
12/16/2014 | 57.67 | 1 | 77.00 | 79.00 | 73.10 |
12/29/2014 | 72.27 | 1 | 72.00 | 73.00 | 69.10 |
2/17/2015 | 57.90 | 1 | 54.00 | 55.00 | 57.90 |
2/26/2015 | 58.27 | 1 | 63.00 | 64.00 | 58.30 |
3/30/2015 | 53.26 | 1 | 91.00 | 92.00 | 53.26 |
6/29/2015 | 50.70 | 1 | 57.00 | 58.00 | 50.22 |
7/30/2015 | 54.08 | 1 | 60.00 | 61.00 | 54.08 |
9/30/2015 | 55.12 | 1 | 61.00 | 62.00 | 56.26 |
10/30/2015 | 58.38 | 1 | 66.00 | 67.00 | 59.22 |
2/18/2016 | 65.80 | 1 | 73.00 | 74.00 | 65.80 |
3/31/2016 | 70.15 | 1 | 77.00 | 79.00 | 70.15 |
4/26/2016 | 67.81 | 1 | 74.00 | 76.00 | 68.60 |
6/25/2016 | 71.15 | 1 | 78.00 | 79.00 | 71.15 |
6/30/2016 | 74.97 | 1 | 81.00 | 83.00 | 75.66 |

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol/Key
- Rating Downgrade
- Rating Upgrade
- Valuation Range Change
- Initial Rating
- Analyst Change
- Split Adjustment
- Outstanding Book
- Underperform/Sell
- Outperform/Buy
- Market Perform/Hold
- Not Rated
- Suspended

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SCG: Risks include regulatory and construction.

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2=Market Perform: The stock appears appropriately valued, and we believe the stock’s total return will be in line with the market over the next 12 months. HOLD
3=Underperform: The stock appears overvalued, and we believe the stock’s total return will be below the market over the next 12 months. SELL

**SECTOR RATING**

O=Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.
M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.
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As of: September 1, 2016

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James von Riesemann
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Price Target Calculation and Key Risks

Our 12-month $84 per share price target is based on a 16.8x P/E multiple on 2018. We also use sum of the parts, single- and two-stage DDM, and price-to-book to help triangulate valuation. Key risks include execution risk with the nuclear project; the cost of building the two new nuclear units is roughly 75% of SCGs market cap today and once complete, will represent nearly one-half the earnings power and two-thirds of the cash flow. General risks include economic conditions, a changing regulatory environment, and changes in interest rates.
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NR: No Rating - not covered, and therefore not assigned a rating.

Rating Distribution
(As of 9/01)

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For disclosure purposes only (NYSE and FINRA ratings distribution requirements), our Buy, Neutral and Underperform ratings are displayed as Buy, Hold and Sell, respectively.

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September 1, 2016

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First Read

SCANA Corp.
Fixing a Deal on a Fixed Price Contract

SCG files settlement with interveners on fixed price nuclear deal
Mgmt successfully filed a settlement with ONS and a variety of other SC parties as part of its petition to increase rates to reflect principally the costs associated with implementing a fixed price deal for its VC Summer nuclear expansion. Hearings are still scheduled for Oct 4 with a decision from the PSC expected in Nov. We see the project as substantially de-risked with this deal; we note the updated CWIP figures reflecting this higher spend were already introduced with 2Q. We look for an update by Oct 1st on the final timing for Construction Milestone payments with Fluor, which could tweak CWIP on the project (hence EPS). The finalization of this schedule should allow for the SC PSC to have the final view on payments by the time it votes.

What are they giving up? No further capital cost increases pre '19
In turn, mgmt. commits to avoid further increases in capital costs pre Jan 28, 2019, just a few months before the scheduled Aug 2019 in-service date of Unit 2 (slight delay from last order of Jun 2019). We note the deal includes interveners with a contingency for project delay of 18-months+ (presumably to line up with the end of ~2020). Experts we've spoken to believe efforts appear under way to provide for a potential PTC qualification extension beyond the 12/31/2020 deadline (potentially indefinitely).

We remain concerned around future project delays
We are wary progress on the site as hiring activities by Fluor ramp and overall productivity appears above 1.0. We believe the project could still be readily delayed, but the question is whether any such delay would be beyond the end of 2020. We note the order only limits the company's ability to file for further increases until 2019, rather than preventing it from doing so. From an investor perspective the limited ability to refile for the time being should substantially de-risk near-term EPS as the SCG will not seek deals beyond the scope defined. A deal was also reached in NC earlier this week.

Also locking in new nuclear ROE at reduced rate of 10.25% through build
Mgmt is also further reducing its ROE on the Summer project to 10.25% from 10.5% (already lowered from 11% from the last deal). Notably this is consistent with SCE & G's currently authorized ROE of 10.25% (to which it would have dropped once reaching in-service anyway). We are not surprised by this aspect of the deal; mgmt also used this lever in the last round of negotiations.

We expect the shares to trade up on deal announcement.
While not additive to 2Q disclosures on CWIP, we think the deal de-risks the shares. We note consensus remains conservative, with this latest deal allowing for positive estimate revisions (albeit offset in part by the slightly lower ROE). Ahead of final payment update on 10/1, we maintain our estimates at the top end of mgmt's 4-6% EPS growth rate; our estimate; are somewhat conservative to reflect the risk of future execution slip.

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Forecast returns

<table>
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<tr>
<th>Forecast returns</th>
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</thead>
<tbody>
<tr>
<td>Forecast price appreciation</td>
<td>+8.6%</td>
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<tr>
<td>Forecast dividend yield</td>
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<td>Forecast stock return</td>
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<td>Market return assumption</td>
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<td>Forecast excess return</td>
<td>+6.2%</td>
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Valuation Method and Risk Statement

Factors that could prevent SCANA from achieving our earnings, cash flow, and price target objectives include: adverse weather conditions; changes in the regional power regulatory environment; adverse regulatory decisions in its various states jurisdictions (primarily SC, NC, and GA) as well as from the federal regulator, FERC; interest rate & capital market risks; slowdown in regional economy; risks associated with operating nuclear units; more stringent environment regulation; and the impact that changes in commodity prices could have on the unhedged portion of its competitive gas business, SCANA Energy. An added risk is the corresponding construction and financial risk associated with its proposed new nuclear units at the V.C. Summer facility. We value SCG on a SOTP using a -5% discount to the peer utility 2018E P/E multiple.
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<th>12-Month Rating</th>
<th>Definition</th>
<th>Coverage</th>
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<td>Buy</td>
<td>FSR is &gt; 6% above the MRA.</td>
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<td>Sell</td>
<td>FSR is &gt; 6% below the MRA.</td>
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<th>Short-Term Rating</th>
<th>Definition</th>
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<td>Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.</td>
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<td>&lt;1%</td>
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<tr>
<td>Sell</td>
<td>Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.</td>
<td>&lt;1%</td>
<td>&lt;1%</td>
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Source: UBS. Rating allocations are as of 30 June 2016.
1: Percentage of companies under coverage globally within the 12-month rating category.
2: Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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<th>Company Name</th>
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<th>Short-term rating</th>
<th>Price</th>
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Source: UBS. All prices as of local market close. Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date.

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SCANA Corp. (US$)

Source: UBS, as of 01 Sep 2016
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