NorthWestern Energy Group, Inc.

Third Quarter 2024 Earnings Call

Presentation

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

Good afternoon, and thank you for joining NorthWestern Energy Group's Financial Results webcast for the quarter ended September 30, 2024. My name is Travis Meyer. I'm the Director of Corporate Development and Investor Relations Officer.

Joining us today to walk you through the results and provide an overall update are Brian Bird, President and Chief Executive Officer; and Crystal Lail, Chief Financial Officer. [Operator Instructions] NorthWestern's results have been released, and the release is available on our website at northwesternenergy.com.

We also released our 10-Q pre-market. So please note that the company's press release, this presentation, comments by presenters and responses to your questions may contain forward-looking statements. As such, I'll direct you to the disclosures contained within our SEC filings and the safe harbor provisions included on the second slide of this presentation.

Please also note, this presentation includes non-GAAP financial measures. Please see the non-GAAP disclosures, definitions and reconciliations also included in the presentation. The webcast is being recorded. The archived replay of today's webcast will be available for 1 year beginning at 6:00 p.m. Eastern and can be found in the Financial Results section of our website.

With that, I'll hand the presentation over to Brian for his opening remarks.

Brian B. Bird
CEO, President & Director

Thanks, Travis. Just real quickly on the recent highlights. We had reported GAAP diluted EPS of $0.76 for the quarter and non-GAAP diluted EPS of $0.65. We are revising our 2024 non-GAAP EPS guidance to $3.32 to $3.47 in light of the delay in Montana interim rates. We're also reaffirming our long-term 5-year rate base and earnings per share growth rate targets of 4% to 6%.

From a dividend declared perspective, $0.65 per share payable December 31, 2024, to shareholders of record as of December 13, 2024. Yellowstone County Generating Station began serving customers in October. In August of 2024, the U.S. Department of Energy awarded $700 million Grid Resilience and Innovation Partnership or GRIP grant to North Plains Connector Consortium project, which included a $70 million earmarked for the Colstrip transmission System upgrades. Of that $70 million, NorthWestern shares $21 million available for our investment in that line.

Turning to the next page, in terms of Northwestern's value proposition, we're still trading today, providing approximately a 5% yield. That, combined with a 4% to 6% EPS growth rate provides a total of 9% to 11% total growth proposition. When you consider on top of that, some activity that we're exploring on the FERC transmission side of our business, providing incremental generating capacity and ultimately some incremental load addition in that line. The ability to continue to look at existing agreements, either from a QF perspective or power purchase agreements for possible buyouts. And just electrification, supporting economic development in our service territories, we believe can provide an 11-plus total growth proposition.

With that, I'm going to turn it over to Crystal to talk about Q3 financial results.

Crystal Dawn Lail
VP & CFO

Thank you, Brian. In my comments today, I will discuss our financial performance for the third quarter combined with our outlook for the remainder of 2024.

As Brian mentioned, GAAP net income of $46.8 million for the quarter or $0.76 per share compares with $29.3 million or $0.48 per share for the prior quarter.

Moving to Slide 9 to provide a bit more detail. As you can see from the quarter-over-quarter analysis, GAAP earnings grew by $0.28. This earnings growth was primarily due to rate review outcomes, transmission revenues and continued strength there and an income tax benefit. Partially offsetting these items was higher insurance costs driven by wildfire coverage. I think you've heard from probably all utilities, the increasing costs to operate our business, particularly on the impacts broadly of wildfire, and we've certainly seen that in our renewed coverage for the year, also higher costs at the depreciation and interest line that were certainly expected in our original assumptions for the period.

A bit more on the income tax benefit reported during the quarter. It is due to the IRS issuing final guidance on gas repairs. Many of you know as well in our earnings, we are a flow through in each of our jurisdictions. And applying the safe harbor method, we recorded a $7 million tax benefit. As this relates to prior periods prior to 2024, we are adjusting this amount out. So you can see the impact in the bridge below as to the drivers for the quarter, again, $0.48 of earnings in the prior period, this quarter, closing on at $0.76 when you remove the impact of that tax repair benefit, you would see $0.65 of earnings over the quarter.

A bit more detail on margin on Slide 10. The primary drivers there are the things we've touched on before, which is the ongoing regulatory execution, driving outcomes in the Montana electric and natural gas case last year. As a reminder, final rates were implemented November 1. So what you see here, impacting Q3 is the lift off of what were the interim rates in place at the time in the prior period. And then also acknowledging our South Dakota electric case, we've had a full year this year of rate improvement there, along with continued growth in our transmission revenues.

Moving to Slide 11. We provide a clear focus on where we're adjusting our earnings. So you can see in Q3 of 2024, the adjustments for weather and other matters are offsetting with the gas safe harbor repairs adjustment of $0.11, the most significant amount were reflecting reducing our net income amount. This compares with a $0.01 adjustment for weather in Q3 2023. So when you look at the results from those 2 that results in adjusted earnings of the $0.65 that our prior -- or mentioned on the prior slide versus $0.49 in the prior period on an adjusted basis.

Moving to Slide 12. As we had updated you on our second quarter call, we executed our financing plan early in 2024 and have shown steady improvement in our FFO to debt metrics and the importance of that to our ongoing credit ratings. Our capital plans remain unchanged, and we continue to expect no equity in our current plans.

Moving to Slide 13, I'll provide an update on why we're thinking about the remainder of 2024. Importantly, our financial performance year-to-date and for the quarter are consistent with our expectations. However, we are revising our guidance, as Brian mentioned, to $3.32 -- a range of $3.32 to $3.47 from what our original range was of $3.42 to $3.62.

I would note, we are navigating a complex regulatory landscape and an election year, and our revised guidance is driven by the delay in Montana interim rates as our original guidance expected interim rates October 1. Customers and the states we serve benefit from the demonstration of a strong regulatory framework as do our owners. That regulatory framework is fundamental to attracting capital and continuing investment in our states.

Many of you have taken note of the denial of interim rates in the MDU proceeding in Montana. Our revised guidance includes interim rate relief in Montana in December. The range of $3.32 to $3.47 reflects at the lower end, no interim rate relief and at the upper end, our requested amount.

Providing a bit more perspective on that and particularly on the electric side, I'll dig in a bit more deep. We believe we have a strong case supporting our request and that our request for interim rate relief is a bit differentiated, specifically on the electric request. This includes both interim, on a base rate perspective and a request for adjustment of the PCCAM base. This is different than in the gas proceeding, where the gas tracker does not become a part of our rate review filings and is just [hidden] separate.

Importantly, captured within the PCCAM adjustment is a bridge rate consistent with similar application in a prior docket, providing for a bridge to final recovery of the Yellowstone generation facility to cover costs until an outcome is determined in the docket. We're very proud of placing that asset into service here and serving customers currently, and we do believe that our request supports fair treatment of that asset.

From an electric total bill perspective, the thing that you should keep in mind is that the downward pressure embedded in that PCCAM request, results in a bill impact in total. So think about electric interim request base rates plus that PCCAM adjustment with the bridge rate is a total of approximately 1% for the combined interim base rate and PCCAM request with the bridge.

Hopefully, the detail we provided here provides a bit more color into how we're thinking about our interim rate request and how that's proceeding. We are confident in a fair outcome in all of our regulatory proceedings that will also enable us to deliver on our commitment of 4% to 6% EPS growth with no equity needs. Our plans for capital investment remain unchanged. I will also note that we plan to provide 2025 guidance following outcome in our Montana rate review.

I'll pass it back to Brian for thoughts on our rate reviews and concluding remarks.

Brian B. Bird
CEO, President & Director

Thanks, Crystal. We provide on Page 15 the rate review summary. I certainly don't plan to go through this column by column, line by line. I guess I would just say this.

Regarding South Dakota and Nebraska, we are continuing -- both of these cases or all of these cases continue to move along quite well, and we do anticipate settling or having outcomes associated with these filings in the first quarter of 2025.

To Montana, I'm sure all of you are aware, there is a procedural schedule that's been established, if you will. And the 2 primary dates of the date shown on this particular slide, I would mention intervenor testimony is expected on January 17 of 2025, and the hearing commences on April 22.

Obviously, the news of the day is around interim. Crystal shared some thoughts on the interim. And I believe the Montana Commission understands the following. First and foremost, more than 80% of our rate base is regulated by the MPSC as compared to something closer to 12% for MDU. So a similar negative outcome for us would be far more consequential to our credit ratings. Secondly, I'd say our interim rates -- our rate requests are for both electric and gas, and is associated with over $1 billion of investment we've made in the state in 2023 and 2024.

Regarding electric specifically, the interim increase to customers, net of bridge rate, as Crystal pointed out, is approximately 1%. And I believe the commission supports our investment in Yellowstone County Generating Station as we try to regain Montana's energy independence.

Regarding gas, the interim increase is closer to about 7% bill increase, but Montana's gas bills will still be lower after this increase than they were last October due to the decline in natural gas prices.

And finally, I believe the commission understands that due to the significant investment in the state, we would have to file more frequently, if not annually without the benefit of interim rates. Everyone understands rate reviews are costly, they're burdensome for all parties involved.

And the other thing to point out that an interim rate increase provides a smaller, more frequent price signal to customers and helps mitigate rate shock. We at NorthWestern are confident the MPSC will consider all of this in their decision on our interim rate request. With that, we'll turn it over to you for questions.

Question and Answer

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

Thank you, Brian and Crystal. [Operator Instructions] With that, we will take our first question from Shar at Guggenheim.

Shahriar Pourreza
Guggenheim Securities, LLC, Research Division

So Brian, obviously, the delayed order with interim rates in Montana impacted the numbers. I guess what's driving the delays. And with your internal planning assumptions now assuming interim rates go into effect in December. I know it's post elections, but what's giving you the confidence there for a December order and can we see further impacts in Q1? I'm still not sure why there's confidence there.

Brian B. Bird
CEO, President & Director

Yes. I would say this. I think you've got 2 rate cases that they're dealing with, with other filings as well in front of the commission. So I can't speak to the timing. Our expectation was when we initially made our filing that we would have, like we had in the last rate case, an outcome around the October time table on interim rates and a successful outcome on interim rates.

I can't necessarily speak for the decisions. Obviously, we had a delay in accepting of our filing initially that potentially caused a delay here. But we still thought interim rates could have been decided in October as a result, even with that delay. So I can't speak to it. I do feel very, very good for the reasons as Crystal pointed out and the reasons, I pointed out why our interim rate filing should be accepted as is.

Crystal Dawn Lail
VP & CFO

And Shar, I would just add on to that in my comments maybe too much detail, but trying to go into the devil of the detail of what makes up those rate requests. And obviously, there's the MDU request is a bit different, more similar to our natural gas side of the house. But our electric side given the PCCAM base can only be reset in a rate review, you have the supply portion, the pass-through supply portion of the bill being taken up on an interim request at the same time and the embedded nature of the interim request related to Yellowstone, I really think makes for different considerations from the commission and thinking about how they're supporting and sending a signal of investment in Montana and supporting what is a plant that is serving customers today and how they go about that.

In the appendix of our materials, we show a bit more granularity into that request. But they -- through that process, will give customers a bill decrease on one piece of it. So I think that's a significant piece of our confidence that the commission will consider all those factors in making a decision in our case.

Shahriar Pourreza
Guggenheim Securities, LLC, Research Division

Got it. That's helpful. And I appreciate that. It's just -- hopefully, the commission does the right thing because it's certainly impacting the cost of capital there.

And then just on the upside opportunities. You guys have had the incremental CapEx buckets for some time. I guess, how should we think about when we could see this in your current through '28 plan, right? So outside of winning sort of the RFPs for generation, what's holding back the other buckets like PPA buyouts and transmission opportunities?

Brian B. Bird
CEO, President & Director

I think it's just fair to say, Shar, that we're in process on working on a number of fronts on these things and things maybe take more time than originally considered. So we're working on things on the transmission front. We're working on things in the generation front and stay tuned.

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

All right. We will take our next question from Chris Ellinghaus at Siebert Williams.

Christopher Ronald Ellinghaus
Siebert Williams Shank & Co., L.L.C., Research Division

So you have to get a notice to proceed to construct something you have to get -- or you have to file notices of intent for rate cases, shouldn't commissions need to make some kind of notification when there is a deadline in the opposite direction, if you have a request for a date or something, shouldn't they at least give you some kind of sense of when they might take something up?

Brian B. Bird
CEO, President & Director

Well, one thing, Chris. I think we did make it very clear in our filings this year after 270 days, we'll be implementing rates. That's one deadline that we can certainly uphold. I believe, through the 20 years I've been here, interim rates historically have come at different points in time. Our belief, though, in terms of the last rate review and the process that was put in place to the last rate review, we had expected something similar here. I can't speak to the rules of the timing here, but I do know that we've had different outcomes and timing associated with interim rates in the past. But more frequent -- more recently, the October would have been a reasonable expectation.

Christopher Ronald Ellinghaus
Siebert Williams Shank & Co., L.L.C., Research Division

Right. So Brian, you sort of alluded to the logic of the interim and some of the parts like Yellowstone that they should have a good comprehension of. But when they look at the stock, if they do at all, and they see a 5% yield, and we're talking about 11% plus sort of total return profile. Do they also recognize that you shouldn't really have an 11% total return profile at this point and where interest rates are. So do you think that they also appreciate that the stock is not reflecting well upon the Montana Commission?

Brian B. Bird
CEO, President & Director

I can't speak for individual commissioners. I'd expect at least on a dividend yield perspective, having a dividend yield closer to 5% when others do not have a dividend yield that high. They should understand that our stock is underperforming versus others. That's as far as I'd go, Chris.

Christopher Ronald Ellinghaus
Siebert Williams Shank & Co., L.L.C., Research Division

Okay.

Crystal Dawn Lail
VP & CFO

Chris, I'll just add on, given we're in the middle of data request responses, and I can't help myself, as Shar alluded to the acknowledgment of cost of capital. And you were asking a question of do folks understand the impact of the performance that we've seen in our stock price and relative to commission decisions.

And I think we'll make that case in spades and continue to do so that you're ultimately -- that strong regulatory contract means less cost for customers because it's a lower cost of capital. The inverse to that is higher cost for customers when you need a higher cost of capital. And obviously, your comments on our stock price and Shar's comments earlier go in that direction.

And we make that case in our data request responses and our testimony, et cetera, to say what's good for customers. We should be able to strike a balance of good for customers, lower cost of capital and good for shareholders at the same time, such that we're providing a reasonable return on folks making a decision to give us capital to invest in states like Montana.

Brian B. Bird
CEO, President & Director

I'll also add, Chris, if you've been covering this company for a very, very long time. You will recall, post-bankruptcy over 20 years ago, that when we didn't have a strong financial picture, our costs from a cost of capital perspective are higher. And as our ratings improved, we could demonstrate to the commission that, in fact, the cost of capital for customers, actually, went down when we had a stronger financial profile. You also understand though that the commission turns over because it's elected commission. So those commissioners are no longer there, may not be aware of that history. So it's on us to certainly educate them.

Christopher Ronald Ellinghaus
Siebert Williams Shank & Co., L.L.C., Research Division

Yes. I would think, Crystal, it's harder to point towards the effect that things -- events like this have on the cost of debt, maybe in the short run, but you could certainly point towards a 150 basis point increase in the cost of equity relative to peers that this certainly doesn't help. So you've got some pretty good data points there.

I wanted to ask about the North Plains Connector. Have you got any update, or can you give us any kind of sense of when you might have a resolution there?

Brian B. Bird
CEO, President & Director

I would say this, we are certainly well positioned at Colstrip with North Plains Connector. As you know, we certainly have good relationships with the utilities to the east of us, we have good relationships with the utilities to the west of us. And obviously, as markets continue to develop, I think our position on North Plains Connector makes good sense. So we are definitely taking that serious. We're evaluating it. We're talking with the folks at Grid United about our interests there.

Christopher Ronald Ellinghaus
Siebert Williams Shank & Co., L.L.C., Research Division

Okay. And one last question. I sort of mentioned that the interim might be partly influenced by the election cycle. That's coming to close here pretty soon. Do you think that once the election is complete, that starts a clock from a political standpoint on when the interim consideration might begin?

Crystal Dawn Lail
VP & CFO

I would just say this, Chris. We have been exchanging data requests with both PSC staff and others. So that's our clearest indicator of where they're moving from a timing perspective. So we do have indication, they're very close to wrapping up their work on an interim recommendation. And I think that's a key piece of what we see as timing. You started your question with is there a shot clock on this thing? Interim rates is a little bit different. But I would tell you based off indications of the data request that we've received, we expect it to be on the docket sometime in November.

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

We'll take our next call from Nick Campanella at Barclays. Yes. It sounds like Richard maybe or Nathan.

Unknown Analyst

Yes. It's actually Nathan on for Nick. So how is FFO to debt trending towards the end of this year given the delay in rates? And do you feel comfortable in meeting your minimums?

Crystal Dawn Lail
VP & CFO

That's a great question, Nathan. And I probably should have noted that in our forecast outlook, and I would say this about our range. I mentioned that the revised range at the low end reflects no interim rate relief. And while we've made important and good strides on solidifying our credit metrics and where we need to be that numerator, as you might imagine, is very sensitive to cash inbound. And without any rate relief in 2024, we will fall back below our downside threshold for 2024. With some interim rate relief as we have expected here from a guidance perspective, think about kind of in the middle of the range. We still wouldn't be quite as good as we are now, but certainly above our downside thresholds.

The other thing that I would just mention, while I'm not giving 2025 guidance, I would acknowledge for 2025, we will not put rates in the earliest of which is likely the 270-day shot clock that Brian mentioned in the response to some of Chris' questions, no interim rate relief during the first 5 months of 2025 would leave us slightly below our downside threshold in 2025 as well.

So the impact to credit metrics, we are making that case to the commission and staff and you're asking the good question of it's certainly a significant impact to us to have invested in the State of Montana to have this much capital we need to recover and we need support from a credit perspective and need that cash on the numerator side to make sure we stay above our downside threshold, but significant impacts both for '24 and '25 from a credit metrics perspective, if we would receive no interim rate relief.

Unknown Analyst

Got It. That makes a lot of sense. And just one more. Do you plan on updating the IRP and generation opportunity now that you have the Yellowstone and rates or that should be coming shortly?

Brian B. Bird
CEO, President & Director

I think 2026 is still the time line from an IRP perspective. Obviously, we continue to watch what's happening at both the federal and state level in terms of needs on a going-forward basis, but 2026 is our current plans.

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

All right. We will take our next call from Julian at Jefferies. Julian, or one of his teammates, I'm guessing.

Unknown Analyst

It's Brian Russo on for Julian. So just on Colstrip and the EPA GHG. Colstrip and the EPA, MATS rules, any update there on retrofitting or retiring? And what are the -- what are the things we should look for going forward in the event that it is retired, where do you think your net short position will be? And how does that impact that incremental CapEx or growth upside that you referenced in your charts?

Brian B. Bird
CEO, President & Director

Yes. I think from a MATS perspective, assuming the rules stay in effect, I think you know, we're involved in litigation there, and certainly, others are, obviously, next week could have an impact on the decisions around MATS as well. We're going to continue to fight that issue. And then if, in fact, we need to move forward with steps of baghouse will be required there.

We believe that, in essence, in order to provide, again, 400 -- a heck of a lot more megawatts associated with the original 222 megawatts to serve customers in Montana. We're going to need to make an investment in a baghouse. And so that's something that I hope we and the commission can get comfortable with on a going-forward basis.

Unknown Analyst

Great.

Brian B. Bird
CEO, President & Director

Back to -- Brian, one thing to take your GHG. It's interesting. I think everyone knows, there's quite a bit of litigation around the GHG rules, too. Obviously, we'll be following those closely. I clearly struggle with those rules, but it's something that we'll have to continue to keep an eye on as well from our investment in Colstrip.

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

And our next call in the queue is from Dylan at Ladenburg Thalman.

Unknown Analyst

It's a question. So should investors consider the outcome of the election is having a bearing on the future operation of Colstrip?

Brian B. Bird
CEO, President & Director

I think I would put it in this context. Certainly, the federal elections have -- could have an impact on the operations of Colstrip. I think the what's required to continue to operate the plant and the ultimate costs associated with continuing to run the plant. I think that I'm less concerned about the in-state elections associated with that. I think we've seen tremendous amount of support within the state legislatively regarding Colstrip. And so I'm certainly more concerned about the federal election at this point.

Unknown Analyst

And say, you guys do invest -- have to invest in a baghouse for Colstrip. Do you like an estimated cost on what that would run you guys?

Brian B. Bird
CEO, President & Director

There's been preliminary analysis in terms of the cost. It's too early for us to provide numbers associated with that cost at this point in time. I think we've shared historically $500 million for 2 baghouses at Colstrip. And still -- we're still under evaluation in terms of the ultimate costs, but it's early innings, and that's where our number is today.

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

All right. Our next question in the queue is from Anthony Crowdell at Mizuho.

Anthony Christopher Crowdell
Mizuho Securities USA LLC, Research Division

I guess just maybe to the question on the baghouse that you guys talked about and then also on the interim rates, maybe it rolls together. I guess, what type of certainty would you need to see from the Montana Commission before you would embark on that large of a capital project with a baghouse?

Brian B. Bird
CEO, President & Director

I think and as part of our existing rate review, there's cost considerations around Colstrip. Obviously, that will give us a very good indication of their support for it. And so after we see that, we can talk more about it at that time.

Anthony Christopher Crowdell
Mizuho Securities USA LLC, Research Division

And then it seems that -- the Yankees did win last night. So if I could use a Yogi Berra quote. It seems like deja vu all over again with following up on Charles' comments with the first question that the last case, I think we were looking for retroactive rates, and it didn't happen. Here, we're up in the air with interim rates, we hope they happen before year-end, or they hope they get instituted.

But just as the company looks forward to given us maybe rolling forward their capital plan, I understand you're 80% Montana, but how much flex is in your capital plan that you could maybe lower capital spending in 1 state and increase in another that's maybe more supportive for the companies on the company's capital plan?

Brian B. Bird
CEO, President & Director

Anthony, that's good questions. You had the last question on the last call, too. I'd say this. I think we're going to get a very good indication if the state wants to be energy independent. And if they want to be energy independent, the utility that provides electricity is 75% of the state, you better support that investment. And if you don't, that's not where we should be investing our dollars. We've had great support in our T&D investment.

And if we're not getting strong signals from the commission to be investing in that space, they will be making the decision that our customers should be more exposed to the market, not Northwestern Energy. So I think there's a crucial point in time for our customers and how the commission reacts to that is going to determine how much we're willing to invest in generation on a going forward basis.

Travis Meyer
Director of Corporate Finance & Investor Relations Officer

All right. With that, we have exhausted the queue, and I'll hand it back to Brian for any closing remarks.

Brian B. Bird
CEO, President & Director

I appreciate, obviously, great questions today. Certainly, concerns from investor standpoint in terms of outcomes from the Montana Commission. And again, reiterating the 80% investment we have there, I certainly have been with this company a long term. I've seen the commission make great decisions for the benefit of customers. I look back to the hydro decision and I think what we would be doing today for our customers without those resources.

And I think what we're trying to do is something similar with what we're doing in the Yellowstone County, Colstrip and ultimately, whatever resource sometime in the future to replace Colstrip, we want to make those decisions. We want to be serving our customers. But you're right, we have to have the right signals from the commission in order to make those investments going forward. And we certainly appreciate your support today. Thank you.