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CANADIAN UTILITIES LIMITED
An ATCO Company

Canadian Utilities Limited
Fourth Quarter and Year End 2022 Results
Conference Call Transcript

Date: **Thursday, March 2, 2023**

Time: **9:00 AM MT**

Speakers: **Colin Jackson** - Senior Vice President, Finance, Treasury, Risk and Sustainability

Brian Shkrobot - Executive Vice President and Chief Financial Officer

Conference Call Participants:

Jessica Hoyle Scotiabank – Equity Research Associate

Alex Kwong TD Securities, Inc. – Equity Research Associate

Operator:

Welcome to the Fourth Quarter and Year End 2022 Results Conference Call for Canadian Utilities Limited.

As a reminder, all participants are in listen-only mode and the conference is being recorded.

I would now like to turn the conference over to Mr. Colin Jackson, Senior Vice President, Finance, Treasury, Risk and Sustainability.

Please go ahead, Mr. Jackson.

Colin Jackson:

Thank you. Good morning, everyone. We're pleased you could join us for Canadian Utilities' Fourth Quarter 2022 Conference Call.

With me today is Executive Vice President and Chief Financial Officer, Brian Shkrobot.

Before we move into our formal agenda, I would like to take a moment to acknowledge the numerous traditional territories and homelands on which our global facilities are located. Today, we're speaking to you from our ATCO Park head office in Calgary, which is located in Treaty 7 region. This is the ancestral territory of the Blackfoot Confederacy comprised of the Siksika, Kainai and Piikani Nations, the Tsuut'ina Nation, and the Stoney Nakoda Nations that include the Chiniki, Bearspaw and Goodstoney First Nations. The City of Calgary is also home to the Metis Nation of Alberta Region 3. We honour and respect the diverse history, languages, ceremonies, and culture of the Indigenous peoples who call these areas home.

Brian will begin today with some opening comments on recent company developments and our financial results. Following these prepared remarks, we will take questions from the investment community.

Please note that a replay of the conference call and a transcript will be available on our website at canadianutilities.com and can be found in the Investors section under the heading Events and Presentation.

I'd like to remind you that all our remarks today will include forward-looking statements, which are subject to important risks and uncertainties. For more information on these risks and uncertainties, please see the reports filed by Canadian Utilities with the Canadian securities regulators.

Finally, I'd like to point out that during this presentation we may refer to certain non-GAAP and other financial measures, such as total segment measures, adjusted earnings, adjusted earnings per share, and capital investment. These measures do not have any standardized meaning under IFRS, and as a result, they may not be comparable to similar measures presented in other entities.

Now, I'll turn the call over to Brian for his opening remarks.

Brian Shkrobot:

Thank you, Colin, and good morning, everyone. Thank you all very much for joining us here today for our Fourth Quarter 2022 conference call.

Before I jump into a summary of our financial results for the year, I just want to talk more generally about our performance, and also highlight a few notable achievements we've had.

First of all, 2022 saw us deliver on significant year-over-year earnings growth. Our Alberta distribution utilities unlocked significant efficiencies that will in turn create meaningful savings for customers going forward. It was also another successful year of operations for our LUMA Energy business, with numerous achievements in the support of the Company's commitment of rebuilding and modernizing the electricity transmission and distribution system in Puerto Rico. These successes ultimately cumulated into the extension of LUMA's supplemental operating agreement, allowing critical work the team is doing for the people of Puerto Rico to continue.

We've also made significant strides in the execution of our energy transition strategy with the completed acquisition of a major renewable generation portfolio and related development pipeline. While continuing to advance a number of our other ongoing energy transition investments, including our Alberta based solar initiatives and our ongoing hydrogen initiatives in the Alberta heartland.

A point that I want to specifically highlight, we advanced a number of Indigenous projects, including supporting the expansion of Denendeh Investments Incorporated, or DII's interest in our Northland Utilities business. Our relationship with DII began in the 1980s and is one of our longest standing indigenous partnerships. This transaction saw them become a 50/50 owner with us in the business.

We're truly proud of these results and the runway they create for us as we look to the future of our business.

Taking this discussion back to our financial performance. Last year was a great year for Canadian Utilities Limited. We achieved adjusted earnings of $655 million, or $2.43 per share for 2022. This is $69 million, or $0.26 per share, higher than the previous year.

While our business overall performed very well in 2022, this growth and year-over-year earnings was primarily driven by the performance of our international natural gas distribution business, and the outperformance achieved in our Alberta distribution utilities as they completed the final year of their second performance-based regulation cycle.

I know many of you have heard me talk about this before. While we're very proud of this financial performance, we are just as proud of our safety performance. At the heart of both our safety and financial performance is the dedication commitment of our employees to excellence.

As we discussed throughout last year, our international natural gas distribution business in Australia benefited from strong operating performance and saw significant earnings uplift related to favorable CPI indexing. This inflation trend carried throughout the remainder of last year and saw the business deliver full year adjusted earnings of $93 million, compared to $65 million in 2021. This is truly an extraordinary performance for the business.

While the ultimate duration of the CPI tailwinds is difficult to predict, current economic forecasts suggest that many of the drivers impacting stronger near-term CPI in Australia will ease into 2023. Current estimates suggest Australia CPI will begin to trend downward to more normal levels in, say, the 3 per cent to 4 per cent range for the year. This will be a key trend to watch and one we expect to realign our 2022 earnings back down to pre-high inflation levels, and to reduce earnings from the segment on a year-over-year basis.

Moving on to our Canadian utilities. The strong performance we saw in our distribution utilities throughout 2022 continued as we closed out the year. It's important to understand that this performance is underpinned by the numerous efficiencies our businesses unlocked during their second PBR term.

Looking ahead to 2023, we will now see these businesses enter a cost-of-service rebasing year where these efficiencies will be shared with ratepayers. We're proud to be able to share these efficiencies with customers at a time when affordability is front of mind for Alberta households, and these efficiencies will translate into an average rate reduction of 6 per cent to 8 per cent for most of our customers.

Despite our Alberta distribution utilities entering a rebasing year in 2023, we still have strong expectations for performance across all of our utilities. The decisions received for our Alberta distribution utilities on their 2023 costs-of-service applications have been positive and support a view that the regulator understands the importance of facilitating a supportive and constructive regulatory framework for this rebasing year.

We know that we also have a strong track record of delivering exceptional ROE outperformance across decades and under numerous regulatory frameworks and structures. Combined with the efficiency carryover mechanism, within our existing regulatory framework, which will allow us to carry forward as much as 50 basis points of outperformance into ’23 and to ’24. We believe we have a solid foundation on which to deliver continued strong performance in 2023.

Beyond 2023, we also know that this cost-of-service rebasing year will be followed by a third five-year PBR term beginning in 2024. We expect decisions related to the key details of this third PBR term later this year.

Speaking more broadly to our regulatory slate for 2023, it's shaping up to be a busy year, and one that looks to reinforce the continued prospectivity that we've seen from the regulator more recently. Decisions on PBR 3, the generic cost of capital proceeding, and our electric transmission general tariff application for years ’23 through ’25 are all expected.

Moving on to capital, I just want to touch on both capital investments we made last year, and also where we're heading in the coming years.

In 2022, we invested $1.4 billion in our business with $1.1 billion of being invested in our core utilities. This ongoing utility investment ensures we have continued generation of stable earnings and reliable cash flows from our utility businesses and drives overall rate-based growth.

In our Energy Infrastructure businesses, we invested an additional $240 million last year, which is an increase of $14 million from 2021. This increased investment reinforces our commitment to energy transition and includes a number of previously announced projects that we are pursuing in this space, including the continued development of our Barlow, Deerfoot, and Empress solar projects, and our Two Hills RNG project, all of which we expect to be completed in 2023; our ongoing hydrogen initiatives in both Canada and Australia; and finally, expansion of our gas storage facilities.

In addition to these greenfield initiatives, on January 5, 2023, we had also announced the successful closing of our renewable generation portfolio acquisition. This acquisition immediately adds 232 megawatts of operating renewables to our portfolio, brings wind generation into our energy mix to complement our existing solar and hydro assets, and includes a development pipeline of more than 1.5 gigawatts of new opportunities.

Not only will this transaction drive cash flows and earnings accretion in ’23, the 1.5 gigawatt development portfolio provides a clear pathway to meeting our 2030 ESG target of owning, developing or managing 1,000 megawatts of renewable energy and will grow our renewable energy portfolio significantly in the coming decade.

In conjunction with the successful closing of this acquisition, we also announced the signing of a long-term renewable energy purchase agreement with Microsoft. This agreement continues to build on the relationship we established with Microsoft through the contracting of our Deerfoot solar development earlier in the year.

Collectively, these agreements and others like them, highlight our prioritization of earnings stability, alongside growth, as we continue to develop a renewable portfolio and leverage the unique Alberta corporate PPA market.

Touching briefly on our larger clean hydrogen production facility project with Suncor, we continue to advance the necessary work to support a move to the front-end engineering design stage in the first half of 2023. Similarly, we continue to progress our work at the Atlas Carbon Sequestration Hub in conjunction with Shell and Suncor and expect to make a final investment decision on the first face of this project in late 2023. While there's significant work still to be done on these projects given their scale, we're excited to continue moving them forward and about the positive signals they send regarding our province’s intentions to decarbonize.

Moving on, our forward-looking expectations for capital investment, we expect to invest $3.3 billion in our regulated utilities over the next three years. While utility operations are the largest contributor to our earnings and will remain so for many years to come, we will also be actively investing in our energy transition growth initiatives in the coming years. Our ongoing hydrogen initiatives with Suncor, our continued pursuit of a potential energy storage investment in Australia, and are successful execution of the acquired 1.5 gigawatts of renewable generation pipeline will all necessitate significant capital investment and drive growth for our business.

Overall, Canadian Utilities have had a phenomenal 2022 that saw us advance key initiatives and growth while delivering strong year-over-year earnings growth for our shareholders. We started the year with the objective of establishing ourselves as leaders in the energy transition space through our ongoing initiatives to modernize the grid and through the new investments made in 2022 related to renewable generation. We've laid a strong foundation to achieve this goal. I'm excited to continue pushing the business and these initiatives forward.

That concludes my prepared remarks, so now I'll turn the call back to Colin.

Colin Jackson:

Thank you, Brian.

In the interest of time, we ask that you limit yourself to two questions. If you have additional questions, you are welcome to rejoin the queue.

I will now turn it over to the conference coordinator for questions.

Operator:

Thank you. We will now begin the question-and-answer session.

Our first question comes from Jessica Hoyle of Scotiabank. Please go ahead.

Jessica Hoyle:

Thanks a lot. I just wanted to start with a little bit on your capital plan for 2023 to 2025. As a utility investment it looks similar to your previous capital plan, and then as you mentioned, there's large jumps for Energy Infrastructure. Can you just add a little bit more colour on those key areas of spend or split between generation and some of your other initiatives and maybe some colour on timing for this additional spend?

Brian Shkrobot:

Sure. Thank you very much for your question. No, if I look at the Utilities, we tend to categorize rate-based growth for both our Canadian and Australian utilities as normal given the mature state of the markets. But moving forward, we see these markets not being—well, expected investment to follow steady growth profile with system reliability and modernization driving rate-based development. Above this, this space investment, we also see significant opportunity for more rapid rate base growth in the energy transition and decarbonization investments to the system. On the electricity side, we expect this to take the form of tie-in infrastructure to integrate additional renewable capacity and energy storage assets along with increases to system capabilities.

Moving on, maybe, to some of the other growth that we see in our energy transition. Obviously, we've been very clear that this is the area where we see significant growth for Canadian Utilities. We've mentioned a few of the hydrogen project, which is multiple billions of dollars, and we have the 1.5 gigawatts of renewable generation portfolio; both, we expect to drive growth throughout the period. Obviously, there's some more decisions and FID decisions to come but we are very excited about the growth opportunities facing the business.

Jessica Hoyle:

Great, thanks for the colour. Given the recent close of the acquisition of the Suncor portfolio, I just wanted to follow up to see if you had any updated thoughts on selling down any assets here or potentially adding a partner to some of your projects?

Brian Shkrobot:

Yes, that's a great question. I think we talked about we have numerous attractive investment opportunities that we're currently pursuing, and Capital Management will be a key focus for us moving forward.

In terms of options, yes, we would consider asset sales, partnering, or even issue of equity. All of them will be explored. We recognize that significant capital will be required to fund these growths and likely beyond our historical sources of capital to execute on that plan, while paying appropriate respect to the maintenance of our credit rating.

I think, historically, we've had strong access to the debt markets, and we expect to continue to do so. In terms of capital recycling, I think we've showed our willingness to do that, whether it's our selling of our legacy Canadian fossil fuel generation business for example, or the sell down of our Alberta powerline project.

As it relates to equity, while this has not been in the past a source of capital funding, it should be also noted that we're not going to shy away from that need for that funding beyond what's available through the other channels to the extent there is significant.

Jessica Hoyle:

Appreciate the colour.

Operator:

Our next question comes from Alex Kwong of TD securities. Please go ahead.

Alex Kwong:

Good morning. This is Alex stepping in for Linda. I have two questions for you today. My first question is on the commissioning of the two Hydrogen projects at the Clean Energy Innovation Hub. Just wondering how these two projects are progressing now that they're in service, and what are your thoughts on the ability to scale hydrogen moving forward?

Brian Shkrobot:

Thanks, Alex. Yes, I think we've been very clear, we do see three pillars of growth in our energy transition, and one of them being clean fuels, and particularly hydrogen. We are progressing a number of our projects, Clean Energy Hub. For example, in Australia, we have started blending in that and the natural gas system there, as well as our refueling stations.

We've announced a number of projects, whether it's recent development, working to export hydrogen to us from Australia to Germany, whether it's our projects here in Alberta, whether blending projects, and as well as just a recent development announcement on working with Qualico on a hydrogen community. Then of course, we have the greater, or larger, project for the Suncor hydrogen facility, which we expect could not only serve local demand, but be available for export. We're very excited, Alex, in hydrogen and continue to be a strong believer in it.

Alex Kwong:

Okay. Great. That's very helpful. My second question is on the delay for the Deerfoot and Barlow projects. I was wondering if you could talk about the causes of the delay, whether its supply chain or labour related, and was wondering if you are seeing these factors impacts your other projects?

Brian Shkrobot:

Yes. Great question, Alex. Yes, in terms of the slight delay and then service dates, they were to supply chain. The team has done an exceptional job to source our panels, and they are all sourced, there was some timing in shipping and delaying it to our location here. But overall, those projects are back on track and expect to be completed—energized by Q3 2023 and commercial operations in Q4 of ’23 for the Deerfoot. The Empress project, we expect construction that started in October ’22, and we expect that to be done and in service by Q4 2023.

Yes, we're seeing some of that, and particularly on our non-regulated projects where we've seen some delay. Obviously, we factor that into our expectations and timing and being very proactive on it.

In our regulated businesses, we haven't seen the same level of supply disruption. That said, our teams are ensuring that they're taking more lead time and procuring material contractors and, overall, we're managing quite well with the inventories that we have.

Hopefully that answers your question, Alex.

Alex Kwong:

Yes, it does. Thanks for answering my questions. I will jump back into the queue. Thank you.

Operator:

This concludes the question-and-answer session. I would like to turn the conference back over to Mr. Colin Jackson for any closing remarks.

Colin Jackson:

Thank you, Ariel.

Thank you all for participating today. We appreciate your interest in Canadian Utilities. We look forward to speaking with you again soon.

Operator:

This concludes today's conference call. You may disconnect your lines. Thanks for participating and have a pleasant day.