NextEra Energy

Utilities
NYSE: NEE
Market Outperform | Hold

September 30, 2023

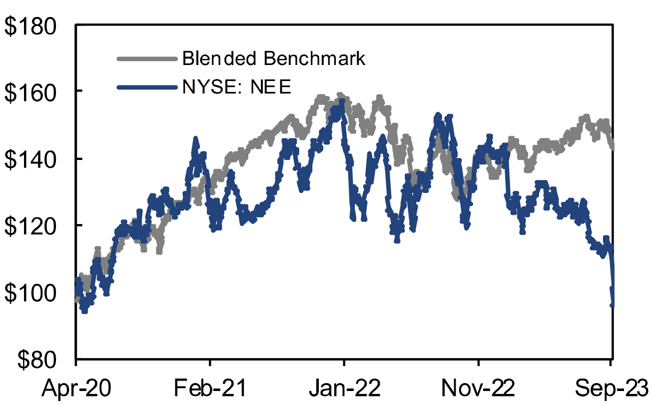
Daniel Krapiwin, Portfolio Manager
Lucas Frame, Portfolio Manager
Jack Demo, Investment Analyst
Lukas Fairley, Investment Analyst

Return on Investment	
Current Share Price	$56.24
Target Price	$75.00
Dividend Yield	3.33%
Implied Return	37%
Conviction Rating	1

Market Profile	
52-Week Range	$47.14 - $88.61
Market Capitalization (US$B)	$151
Net Debt (US$B)	$74
Enterprise Value (US$B)	$225
Beta (5-Year Monthly)	0.54

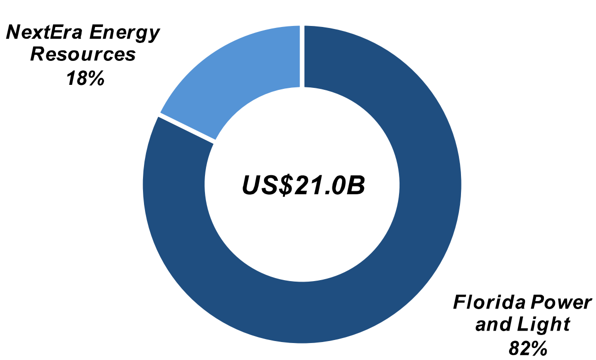
Metrics	2023E	2024E	2025E
Revenue (US$mm)	$26,012	$26,999	$29,274
EBITDA (US$mm)	$13,804	$14,889	$15,723
EPS (US$)	$3.13	$3.40	$3.65
EV/EBITDA	16.3x	15.1x	14.3x

Holding Period Trading Performance (Indexed to $100)



Source: S&P Capital IQ

Figure 1: 2022 Segmented Revenue Mix



Source: Company Filings

Business Description

NextEra Energy (NYSE: NEE) is a clean energy generation, transmission, and distribution company based in Juno Beach, Florida. The Company is segmented into two main businesses: Florida Power and Light (FPL) and NextEra Energy Resources (NEER). As of December 2022, FPL is the largest electric utility in Florida with ~34GW of generation capacity, 88,000 miles of transmission, and serves over 12 million people through approximately 6 million customer accounts. FPL invests in generation, transmission, and distribution facilities to deliver highly reliable and low-cost energy to end consumers. NEER's strategic focus is developing, constructing, and operating long-term renewable contracted assets in the U.S. and Canada. ~92% of FPL's energy mix consists of natural gas and nuclear generation, while NEER's energy mix is 96% renewable.

Industry Overview

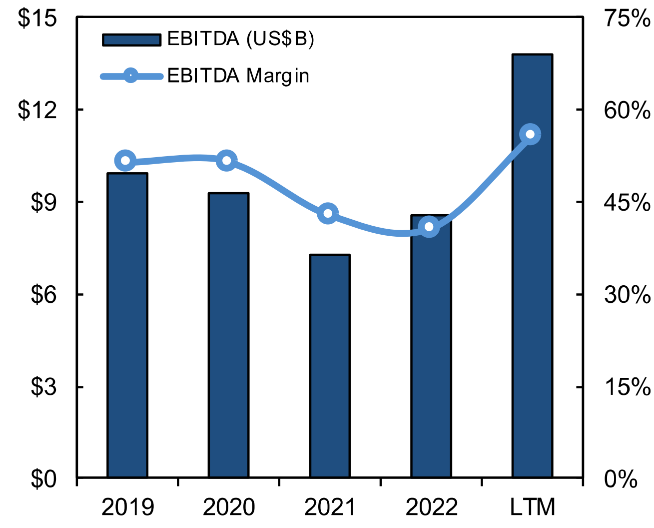
The utilities industry is segmented into four main business units: (1) Electric Power Transmission and Distribution, (2) Electric Power Generation, (3) Natural Gas Distribution, and (4) Water, Sewage and Other. NEE operates in the electric power transmission and distribution and electric power generation segments, competing with peers such as Duke Energy Corp (NYSE: DUK), ReNew Energy Global PLC (NASDAQ: RNW), Southern Company (NYSE: SO), Algonquin Power & Utilities (TSX: AQN), and Northland Power (TSX: NPI). Electric Power Transmission and Distribution is highly regulated, with federal bodies setting the rates at which utility companies can charge consumers. These rates are set to recover any development, construction, and operational costs the Company realizes, while allowing for a modest rate of return while maintaining consumer affordability.

As the world transitions its energy supply to sustainable resources to meet net-zero targets, demand for clean energy projects such as renewables and LNG has increased. Across the Electric Power Generation segment, power prices have risen slower than inflation due to a surge in renewable assets. This has put pressure on sponsors when developing projects, while inflation has caused cost overruns on new projects. As a result, it has been more difficult for smaller companies with lower access to capital to compete on a large scale. However, with the introduction of the *U.S. Inflation Reduction Act* (IRA), renewable power projects have been heavily incentivized through investment and production tax credits, accelerating the transition and driving the industry forward.

Development Pipeline and Growth Strategy

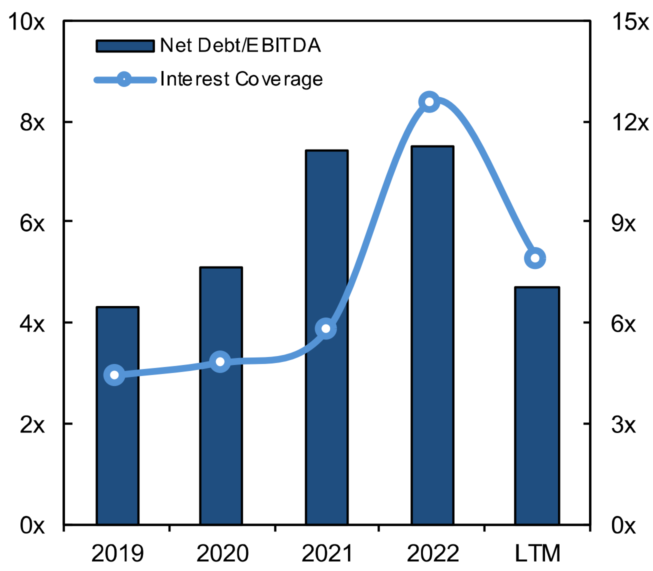
NEE brought ~1.0GW of renewable generation and storage into operation over the third quarter. It also added ~3.2GW of generation and storage to its backlog, which now totals ~21.0GW. This addition to the Company's backlog includes ~0.4GW of wind generation, ~1.5GW of solar generation, ~0.9GW of storage, and ~0.5GW of wind repowering. NEE's growth plan includes funding growth through the sale of its Meade and Texas pipelines to third parties. The proceeds from these sales will be used to fund asset repowering and third-party acquisitions over the next five years.

Figure 2: LHS EBITDA vs RHS EBITDA Margin



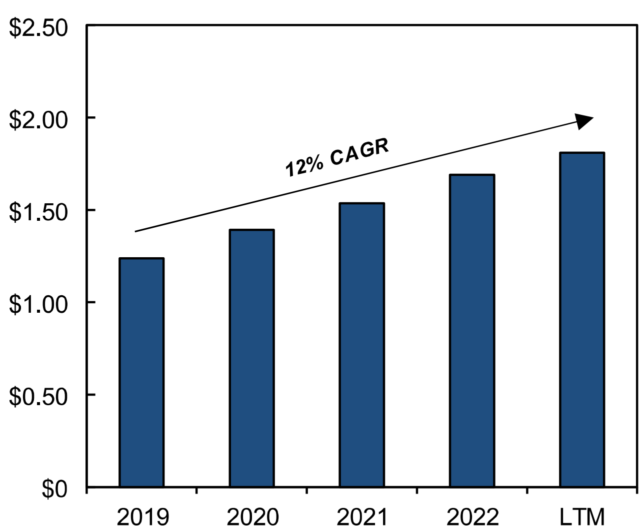
Source: S&P Capital IQ

Figure 3: LHS Net Debt/EBITDA vs RHS Interest Coverage



Source: S&P Capital IQ

Figure 4: Dividend Per Share Growth (US$)



Source: S&P Capital IQ

Mandate Fit

Quality Management: John Ketchum was appointed as CEO and Chairman in 2022. Since joining the Company in 2002, Ketchum has also served as president and CEO of NEER and CFO of both FPL and NEE. Since becoming CEO, Ketchum has exercised disciplined capital allocation, focusing on reinvesting into NEE's core assets. NEE's CEO compensation package consists of 90% at-risk pay, of which a majority is tied to long-term performance, whereas NEO compensation consists of 15% at-risk pay. Additionally, 92% of the Company's Directors are independent, and 31% of its board membership are female and gender diverse.

Competitive Advantage: NEE's competitive advantage resides in its ability to deliver competitive pricing and reliable distribution for consumers in Florida, further establishing its position as the state's leading energy provider. NEE benefits from a first-mover advantage in the renewables market while continuing to exercise its broad scope of regulated operations. This translates to the Company's North American operations, where it is one of the largest electric and energy infrastructure companies. NEE leverages its expertise by expanding into diversified revenue streams across markets in its FPL and NEER segments. The Company's dominant position in the clean energy industry, vertical integration, and geographic diversification has positioned it as a leader in clean energy production and distribution. The Company has an operating efficiency ratio of 37%, compared to its peer average of 24%. In Q3 2023, NEE reported EPS growth of ~11% YoY, compared to peer EPS growth of ~7% in the comparable period.

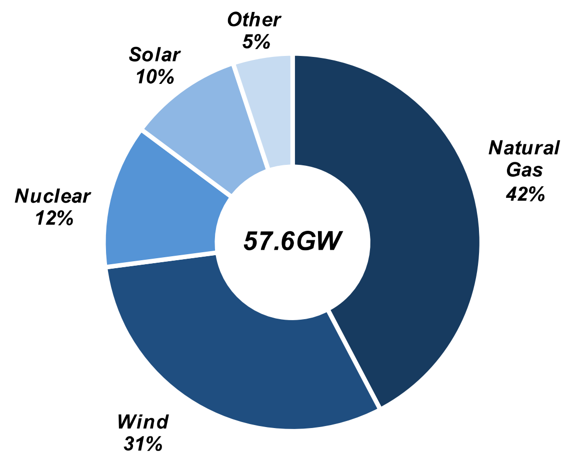
Strong Balance Sheet: NEE achieves financial strength through its size and scope of operations, advantageous market positioning, and strong credit quality in its regulated and renewable segments. The Company holds credit ratings of A-, Baa1, and A, from S&P, Moody's, and Fitch, respectively. The Company's FFO/Debt of 19.2%, has been above the downgrade threshold of 18.0% from S&P for the last five consecutive years. NEE holds a Net Debt/EBITDA ratio of 4.6x, below the peer average of 5.6x. NEE's regulated power segments of FPL have been the financial anchor of the Company, providing credit risk mitigation through long-term contracts and dependable revenues from a diversified clientele. Due to the rate-sensitive nature of the industry, NEE is prone to fluctuations in the economic viability of certain capital projects. Given that the Company has entered ~US$20.5B of interest rate hedges, a 50bps upward shift in the yield curve would not materially impact adjusted EPS in 2023 and 2024. The tenor of swaps are between five and ten years, with a weighted average rate of ~3.8% this allows the Company to mitigate interest rate impacts on its backlog debt maturities from 2024 through 2026.

Growing Free Cash Flow: The Company's capital expenditures represented ~93% and ~91% of revenue in 2021 and 2022, respectively. NEE announced Q3 2023 capital expenditures of US$13.2B, of which ~US$6B is allocated towards the modernization of FPL's transmission and distribution assets. The remainder is allocated towards the Company's growth plan, consisting of legacy asset divestitures for the development of new, high-growth assets. NEE has a five-year CFO CAGR of 4.92% and has generated stable cash flows through its utility-scale generation portfolio and contracting abilities.

Catalysts and Risks

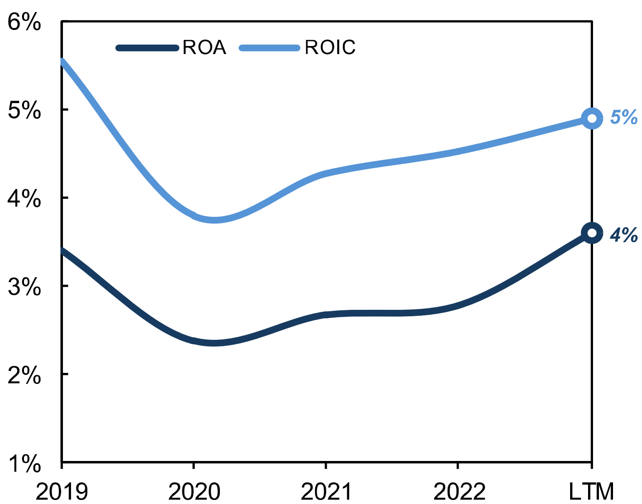
NEE's three primary risks include: (1) reduced regulatory (cont.)

Figure 5: 2022 Generation Capacity by Fuel Type



Source: Company Filings, S&P Capital IQ

Figure 6: ROA & ROIC



Source: S&P Capital IQ

incentives, (2) adjustments to its allowed level of return on equity, and (3) the inability of NEE to sell its legacy pipeline assets.

(1) NEE relies on government and regulatory incentives to develop its utility-scale renewable generation portfolio. This includes tax credits, grants, or legislation favorable to renewables and green energy generation.

(2) Judicial changes to NEE's return on equity could impact the Company's ability to generate revenue and result in a decreased ability to achieve the Company's 6% growth plan.

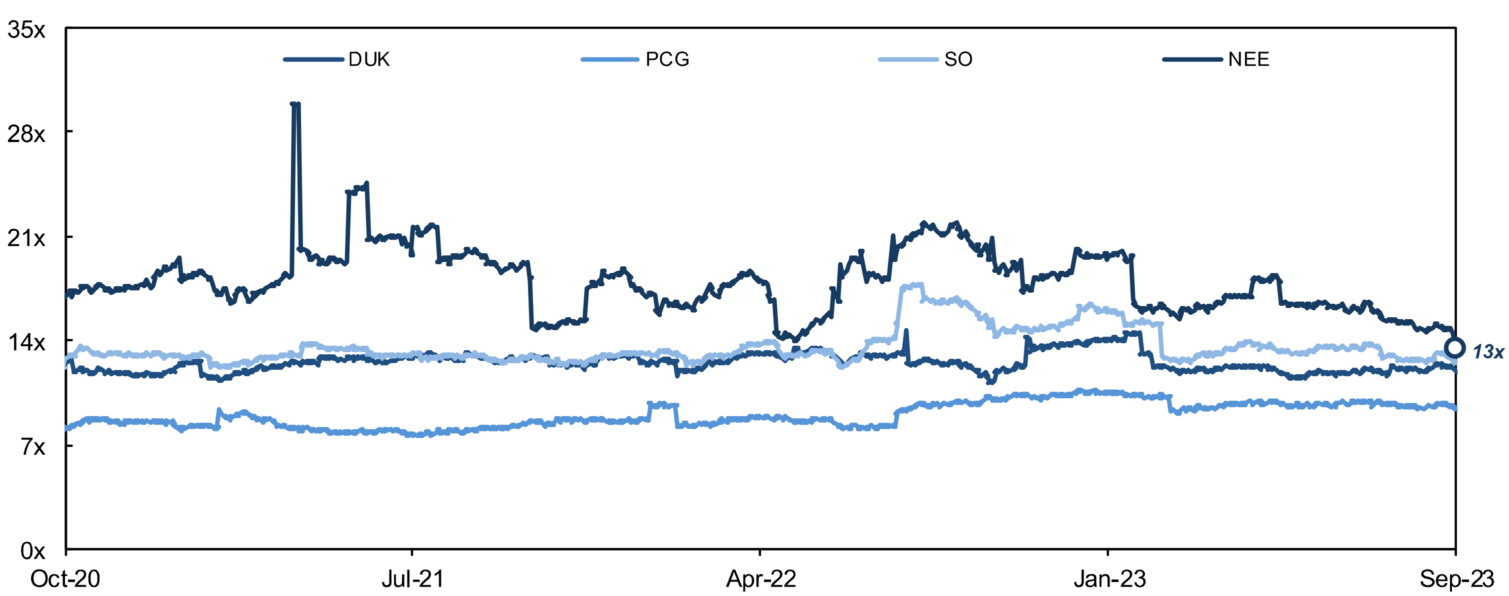
(3) The Company has plans to fund parts of its long-term growth strategy by selling its legacy pipeline assets in Texas and Pennsylvania. This includes its growth equity requirements. If the Company is unable to do so, NEE may need to turn to more expensive sources of financing to fund its growth.

The Company's catalysts are derived from Florida's population and housing growth, which drives its FPL revenue. FPL added ~65,000 new customers in Q3 2023, representing a 1.1% increase YoY. Florida building permits, measured by a three-month moving average, were ~17,000 as of Q3 2023, a decrease of ~2,000 YoY. As Florida's Q3 retail sales increased 3.0% YoY, the Florida economy remains healthy and continues to be the fastest-growing state in the country.

Investment Thesis and Valuation

The CPMT valued NEE at $75 using an eight-year DCF with a WACC of 7.5%. The terminal value was derived using a blend of (1) an 11x EV/EBITDA multiple and (2) the Gordon Growth method using a 1.0% terminal growth rate. The CPMT initiated its position in NEE in April 2020 with a thesis that the Company will leverage its competitive positioning in the regulated utilities industry to expand its high-growth renewable platform. With the implementation of the IRA and a Tax Credit structure in Canada, NEE is now more solidified to expand its renewable and energy infrastructure portfolio. Its large development backlog secured by long-term PPAs will provide sustainable growth with steady cash flows. Overall, the Company's best-in-class operations, accompanied by recent drawdowns in valuation due to interest rate increases, provide an opportunity to rebalance NEE in the portfolio.

Figure 7: NTM EV/EBITDA vs Peers



Source: S&P Capital IQ