

# LONG-TERM VALUE

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As natural gas reasserts its role in the energy mix, utilities are talking up their positive investment potential.

BY M. DIANE MCCORMICK

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**N**atural gas utilities deliver long-term value through rate-base growth, customer service, emissions reductions and innovation. It's a great story, and investors are listening.

“We’re part of the solution going forward from a viewpoint of reliability, safety and environmental performance,” said Adam Woodard, treasurer at Spire. “It’s all tied together. We’ve seen that picked up and recognized by investors.”

With long-term growth in earnings per share projected in the 5% to 8% range through 2027, natural gas utilities are optimistic. Their ongoing strategy? Infrastructure modernization that delivers sustained growth, along with investment opportunities in cleaner energy and emissions reduction, both of which are positioning gas utilities as essential contributors to a net-zero future.

**Renewed Appreciation**

Until recently, gas utilities were grappling with an optical “terminal value issue” among investors, who saw a system facing obsolescence, said Shar Pourreza, senior managing director, North American power/utilities, Guggenheim Partners LLC.

But a string of circumstances changed that outlook. Destructive storms wreaked havoc on power and energy systems across the country. Coal-fired and nuclear power plants closed, causing the loss of many reliable, baseload-capacity resources. Russia invaded Ukraine, reviving fears about threats to energy independence, security, diversity and adequacy.

“People said, ‘Wait a minute. You can’t really run the system on batteries and various intermittent resources, and we kind of need our gas utilities, whether it’s pipelines or gas distribution systems, to maintain integrity and reliability,’” said Pourreza. “That’s where sentiment has shifted.”

In storm-wracked states, political support often solidifies around hardening power systems to ensure reliability, said Sarah Akers, director, equity research—utilities, Wells Fargo Corporate & Investment Banking. In its wake, investors see good investment opportunities “that are aligned with the state, that should be treated fairly and, in rate cases, get recovery and earn a fair return.”

Natural gas utilities are stepping up with proactive measures proving their importance in the 21st century’s changing energy landscape. In 2022, NiSource initiated a strategic business review, identifying opportunities for driving value to shareholders while retaining customer affordability. During plans for attaining net-zero and welcoming new CEO Lloyd Yates, the time was right to optimize the company’s cost profile and scrutinize operations from a fresh perspective, said Shawn Anderson, senior vice president, strategy & chief risk officer.

“Digging into our businesses and retesting our assumptions around how they’re performing provided us the opportunity to dive into all the fundamentals we can to really provide value,” he said.

## Tracking the Clean Energy Conversion

Investors may be interested in clean energy conversion and net-zero goals, but infrastructure investment remains the biggest driver, said Akers. Analysts aren’t seeing significant differentiation in gas utility valuations and multiples closely tied to environmental, social and governance policies, she said: “Investors want to see a decarbonization story out of the companies, but they are OK with the traditional gas pipe replacement story as well.”



Duke Energy developed a first-of-its-kind methane-emissions platform that measures real-time methane emissions in natural gas distribution systems using satellites, sensors and other technologies—a first for natural gas utilities.

PHOTO COURTESY OF DUKE ENERGY

Still, ESG adds valuable context to the picture of natural gas as a solutions provider. Natural gas helps satisfy demand for new energy and decarbonization while sharing its existing and expanding infrastructure for cost-effective distribution, said Anderson. NiSource, he noted, maintains an intentional focus on maximizing value creation in everything it does.

“This approach allows us to ensure reliability while still incorporating these sustainable energy supplies, which is exactly what ESG is focused on, to ensure that we are strengthening our communities,” Anderson said. “We’re spurring economic development, and we protect the systems that are already in place so customers can afford a clean energy transition in a timely manner.”

Duke Energy remains committed to sustaining natural gas as a choice within a diverse energy mix, said Sasha Weintraub, senior vice president and president, natural gas business. “Natural gas is something our customer chooses to have,” he said. “A lot of people like natural gas in their homes and businesses.”

Duke, like other utilities, is also sharing how natural gas plays a role in clean energy. Duke Energy is striving to achieve net-zero Scope 1 methane emissions from its natural gas system by 2030, plus net-zero Scope 3 upstream emissions from purchased natural gas and downstream emissions from customers’ consumption of natural gas sold by 2050. Tactics include energy efficiency, voluntary renewable natural gas and carbon offset purchases, and detection of methane leaks via satellite.

“This appeals to investors because it shows that natural gas can be a part of the clean energy future if we’re able to eliminate methane leaks off our system,” said Weintraub. “When we piece all that together, it’s a great story.”

At NiSource, its net-zero goal demonstrates that continued execution of its long-term business plan will drive greenhouse gas emission reductions while ensuring a safe and reliable supply of energy to customers, said Anderson. That plan incorporates multiple zero-commodity cost solutions, such as RNG, electric and gas facilities, and solar facilities.



NiSource’s Shawn Anderson spoke with investors at Investor Day in New York City this past November.

PHOTO COURTESY OF NISOURCE.

“Long-term, we believe we’ll need constructive legislation and constructive policy, and we need marketplaces to ensure that some of these technology solutions can be affordable for our customers,” said Anderson. “But we see the pathway forward, with that being very consistent with the infrastructure modernization programs and the innovation that’s already coming into place in the marketplace today.”

NiSource also leverages technology to pursue customer affordability and investment opportunities. In its own satellite emissions detection tests, said Anderson, NiSource sees a “win-win-win”: It’s assuring reliability, accelerating Scope 1 and Scope 2 decarbonization goals, and pairing shareholder value with rate-based investment opportunity.

## **RNG’s Role**

Also on the clean energy side, RNG procurement and production, where deployed, appeal to gas utilities because they don’t require significant infrastructure upgrades, said Akers. Now, some new state laws could make direct investments in the space even more attractive by allowing rate-based recovery of investments in RNG facilities and other alternatives.

At Duke Energy, it is already minority owner of a dairy RNG systems builder, part of a five-year plan to be a leader in RNG. A new Tennessee law allowing rate-based recovery of investments in innovative alternate fuels, plus a tax credit created in the federal Inflation Reduction Act, is enhancing RNG’s financial feasibility.

“We’re showing that these are prudent investments, and the gas produced can be equal to or lower cost than geological gas,” said Weintraub. “As states see that RNG doesn’t have to be a premium, we’re excited that other states will follow with legislation allowing for this type of regulated investment.”

In Missouri, Spire is likewise reviewing opportunities to use new legislation that encourages the regulated development of RNG, said Woodard.

Meanwhile, the states where NiSource operates local utilities—Indiana, Ohio, Kentucky, Pennsylvania, Maryland and Virginia—constitute a constructive environment much appreciated by investors. It's one where policymakers and regulators encourage innovations in emerging fuels and other pro-business initiatives that support both economic development and decarbonization. “We believe over time the proof set in these demonstration projects and the reshaping of the marketplace around the customer reliability of these energy products will help drive their development,” said Anderson.

As the successor to RNG, hydrogen is “hyper interesting” as utilities nationwide conduct pilot tests into possible blends, said Pourreza, but “no one wants to be a first mover.” Hydrogenpowered generation, being explored as a scalable pathway for decarbonization, is “probably eight to 10 years out,” he said.

While some utilities are pushing the boundaries in hydrogen, major investment dollars haven't materialized “in a meaningful way,” said Akers.

Much like renewable energy tax credits helped reshape the U.S. marketplace for wind and solar, incentives in the Inflation Reduction Act and Infrastructure Investment and Jobs Act could help make hydrogen more affordable for pipeline use, said Anderson. NiSource—currently participating in three hydrogen hubs—is also pilot testing hydrogen blends to ensure excellent service levels and reliability can be maintained “should something like hydrogen become much more affordable in a larger scale for our customers in our distribution systems.”

## Pipes and People

Still, capital expenditures at natural gas utilities are driving much of the growth in natural gas utilities, said Akers. Investors appreciate the regulatory backing behind pipeline safety and modernization, and they especially like the “nice, long runway” afforded by gas utilities projecting capital investments 10 or 15 years into the future.

While residential customer growth is another favorite investor metric, NiSource is mining growth opportunities among manufacturing and industrial facilities as they operate and expand in the U.S. NiSource is playing the role of convener, particularly in the Midwest, gathering sophisticated actors to develop innovative fuel products, including hydrogen.

“Investors are starting to understand that customer growth isn’t necessarily just about meter counts any longer,” said Anderson. “Instead, some of these larger industrials can represent in the aggregate form just as much growth, and certainly on a sustaining basis, because these are companies making investments for decades into the future, extending our system and prolonging the use of the energy itself. It also provides a baseline for more residential to locate in and around these areas.”

At Spire, rate-base growth has been largely predicated on a long-term plan to replace pipes. “We need to make sure the system is safe and reliable, but at the same time, we want to preserve the affordability of our essential service,” said Woodard. “We target keeping the growth in rates at or below the rate of inflation.”

As utilities note—and Akers agrees—infrastructure investments also support emissions-reduction goals. “These investments are the key to lowering our emissions footprint,” added Woodard. “They’re part of our commitment to maintaining the safety of our system and have a positive environmental impact as well.”

Like utilities nationwide, Duke Energy’s customers are reaping the benefits of compliance with the Pipeline and Hazardous Materials Safety Administration’s 2011



call to accelerate upgrades to pipeline infrastructure. When a major winter storm struck its Tennessee, Ohio and Kentucky service territories around Christmas 2022, the utility had its largest-ever send-outs of natural gas, “and we were able to operate perfectly well,” said Weintraub. “We continue to make sure our system can meet our customer needs on the coldest of winter days.”

Regulators believe in diversifying the energy mix and shepherding the successful evolution of decarbonization pilot programs, but they also tell Pourreza that, first, customers want to keep services functioning. Second, they want to keep rates in line. Regulators reviewing spending programs must “balance the infrastructure need with the customer bill impact.”

Investors are watching today’s high interest rates, too, Pourreza added. When interest rates rise, so does the cost of debt, which passes through to consumers and affects bill headroom, “just like natural gas prices,” he said. “And eventually, it could curtail spending programs.”

Akers confirmed that investors are keeping a close eye on the pressures squeezing customer bills for natural gas and household expenses. They haven’t taken steps to disinvest, but they spent much of 2022 asking whether utilities would pull back on their spending plans.

“The investment should stand on its own merits, but at the end of the day, it’s difficult for regulators to close their eyes to the entire bill and the impact of their decisions on consumers,” said Akers. “There does tend to be a sensitivity and that balance to make sure that they encourage infrastructure investment but also remain cognizant of the customer bill, and that becomes more challenging when commodity prices are on the rise.”

## Good Governance

Spire is working to deliver the cost-saving benefits of natural gas to customers of all income levels, said Woodard. This includes implementing operational efficiencies and investing in technology to help keep bills down and deliver enhanced customer service. The combination appeals to investors.



Spire crews in Birmingham, Alabama, and other communities are supporting pipeline modernization, which is further enabling the utility to reach emissions-reduction goals.

PHOTO COURTESY OF SPIRE

“Looking at different ways to think about what we’re doing and how we’re doing it, the question is whether we can do it more efficiently,” said Woodard. “How can we

keep delivery costs low in the face of rising costs?”

Such gathering of resources to weather the headwinds of a volatile economy signals analysts to issue their “hold” and “buy” recommendations, said Pourreza. When the challenges of inflation, interest rates and commodity prices rear their heads, gas utilities with other levers in their plans—whether in operations and maintenance, efficiencies, load growth, new home connections, propane conversions or other aspects—can demonstrate capabilities to withstand the blows.

This period is “a really fascinating time” for finding improvements in affordability, reliability and sustainability, said Weintraub. Investors are marveling over satellite methane detection while also viewing RNG as a means to offset carbon emissions and “displace geological gas with better carbonintensity fuels.”

“It’s exciting,” he said. “I think investors appreciate everything we’re doing. When they hear what we’re doing and hear that we’re making investments, they have confidence that we can be part of that clean energy future.”