Black Hills Corporation (Q3 2024 Earnings)
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Corporate Speakers

- Salvador Diaz; Black Hills Corporation; Director of Investor Relations
- Linden (Linn) Evans; Black Hills Corporation; President and Chief Executive Officer
- Kimberly Nooney; Black Hills Corporation; Senior Vice President and Chief Financial Officer
- Marne Jones; Black Hills Corporation; Senior Vice President, Utilities

Participants

- Andrew Weisel; Scotiabank; Director, Sell-side Equity Research
- Christopher Ellinghaus; Sibert Williams Shank; Managing Director
- Brian Russo; Jefferies; Analyst

PRESENTATION

(Operator Instructions)

Salvador Diaz^ Thank you. Good morning. Welcome to Black Hills Corporation's third quarter 2024 earnings conference call. You can find our earnings release and materials for our call this morning, on our website at www.blackhillscorp.com under the Investor Relations heading.

Before we begin today, we would like to note that Black Hills will be attending the Edison Electric Institute's Financial Conference on November 10 through November 12. Our leadership team will be meeting with investors and analysts at the conference and the investor presentation will be posted on our website prior to the event.

Leading our quarterly earnings discussion today are Linn Evans, President and Chief Executive Officer; Kimberly Nooney, Senior Vice President and Chief Financial Officer; and Marne Jones, Senior Vice President, Utilities.

During our earnings discussion today, comments we make may contain forward-looking statements as defined by the Securities and Exchange Commission and there are a number of uncertainties inherent in such comments. Although we believe that our expectations are based on reasonable assumptions, actual results may differ materially.

We direct you to our earnings release Slide two of the investor presentation on our website and our most recent Form 10-K -- Form 10-Q filed with the Securities and Exchange Commission for a list of some of the factors that could cause future results to differ materially from our expectations. I will now turn the call over to Linn Evans. Linn?

Linn Evans^ Thank you, Sal. Good morning. Thank you, all for joining us today. I'll begin my comments with a brief overview of the quarter. Kimberly will provide our financial update, and Marne will provide more detail on our team's operational performance and our strategic progress.

Starting on Slide 3. We I'm pleased with our progress on our customer-focused strategy, which is reflected in new margins and the advancement of our growth projects. As a team, we delivered excellent service to our customers, continue to execute on our financial targets, and advanced our regulatory and growth initiatives.

We continue to deliver on our commitment to provide our customers with safe and reliable service during the quarter including dependable energy delivery through near peak demand levels for our South Dakota electric system. Despite unplanned generation outages, total availability for our fleet remained above the industry standard with 98% availability for our natural gas units, and 95% total availability across our generation facilities.

We also took the opportunity to bring forward and complete some future major maintenance on units that experienced unplanned outages. The reliability we deliver to our utility customers this quarter was excellent.

Our focus on reliability is delivering value for all of our customers and is a key value driver in attracting new customers to our service territories. During the third quarter, we announced our plans to serve Meta's first data center in Cheyenne, Wyoming, starting in the 2026 timeframe.

As we look to the future, we are excited to serve demand for hyperscalers with our capital-light model and continue to receive inbound requests to expand load beyond Cheyenne. We remain on track with our $800 million capital plan for the year.

Our ongoing capital investment plan is critical to delivering upon the commitments we made to serve our customers and communities safely, reliably and cost effectively. This includes our ready Wyoming electric transmission expansion project which strategically interconnects our Wyoming and South Dakota transmission systems, enhancing the resiliency and capacity of our regional energy infrastructure. Notably, this will benefit our customers with cost stability and expanded energy market access.

Maintaining our solid financial position remains a focus. We reached key milestones in our financial plan as we achieved our debt to capitalization target to maintain our BBB+ or equivalent credit rating. Our team completed our major financing needs for the year as we execute our strategy in funding our customer-focused growth.

During the third quarter, we advanced our regulatory initiatives. We received approval of new customer rates for Arkansas Gas, which were implemented in October. We achieved a settlement for our rate review request at Iowa Gas, which is pending commission approval and we continue through the regulatory process for new rates at Colorado Electric.

We're currently targeting a cadence of three to four rate reviews annually, driven by our investments to serve our customers' growing energy needs. We remain confident in our financial outlook provided on Slide 4. We're on track to deliver on our earnings guidance range of $3.80 to $4.00 per share as originally issued in February.

Our financial performance for the quarter and year-to-date were in line with our expectations as we successfully mitigated the impacts of mild weather, unplanned generation outages and increased insurance expense.

We entered the peak heating season with new rates or interim rates in place at four of our six gas utilities this year. Looking ahead, our strong growth opportunities and continued execution of our initiatives gives us confidence in achieving our long-term 4% to 6% EPS growth target.

Slide five displays our current five year capital investment plan. Over our five year plan period, we expect to invest $4.3 billion. In 2026, our $1.3 billion forecast includes generation investments resulting from our recent electric resource plans. As contracts are negotiated, timing of these investments will be updated. Marne will cover the status of our resource plans and her business update.

In 2027 and 2028, we anticipate incremental opportunities to be added to our plan as we gain more clarity around timing, costs and the energy needs of our customers as indicated by the green arrows above the chart. As a reminder, at our fourth quarter earnings call in February, we will provide our 2025 earnings guidance and an updated capital forecast through 2029.

Slide 6 provides a summary of our hyperscale data center and blockchain growth opportunities. For more than a decade, we have successfully served Microsoft's data center energy needs through a capital market energy procurement model. Our innovative tariff is instrumental in enabling a win-win of efficiently procuring market energy while providing a return in lieu of new generation investment.

We continue to expect earnings from this type of customer to grow EPS contribution from 5% in 2023 to more than 10% of total EPS by 2028. In summary, before I turn the call over to Kimberly, I'm pleased with our strategic progress. Our service territories are stable and growing with strong electric and gas investment opportunities. Our financial position is solid, and we are executing on regulatory recovery as we pursue our growth initiatives. With that, I'll turn the call over to Kimberly for our financial update. Kimberly?

Kimberly Nooney^ Thank you, Linn. And good morning, everyone. As Linn mentioned, third quarter results were in line with our expectations, and we are on track to deliver on our earnings guidance and financial targets for the year. We completed our key financing activities and achieved our net debt to capitalization target of 55%.

We are executing on our strategy to deliver on the financial commitment we made to grow our compounded annual EPS growth rate by 4% to 6%. Despite mild weather and other unexpected cost pressures this year, we are delivering new margins and managing our costs to achieve our financial objectives.

Slide 8 shows third quarter EPS drivers compared to the same period last year. We reported $0.35 per share compared to $0.67 per share in Q3 2023. New margins were offset by higher operating expenses, unplanned generation outages, lower off-system sales and prior year one-time benefits.

We delivered $0.16 of new margins including new rates and rider recovery of $0.10 per share from our electric utilities, $0.05 from our gas utilities and $0.01 per share of customer growth and usage. These positive margin drivers offset unplanned generation outages, lower off-system sales and a prior year benefit from insurance proceeds.

O&M increased $0.23 comprised of $0.15 from higher insurance premiums, employee costs and outside services, $0.03 of expenses associated with unplanned generation outages and $0.05 due to a prior year gain on sale of land to a data center customer.

Interest expense increased $0.05 per share, driven primarily by higher interest rates while new shares lowered EPS by $0.02. Depreciation expense increased $0.05 per share due to new assets placed in service.

Slide 9 displays the earnings drivers year-to-date through Q3 2024. Through three quarters, we delivered a total of $0.57 per share of new margins driven by the successful execution of our strategy. These new margins include $0.35 per share of new rates and rider recovery from our gas utilities and $0.17 from our electric utilities, which includes data center demand.

Additionally, we continued to experience customer growth and increased usage, which contributed $0.05 per share of margin. This margin growth was partially offset by lower off-system sales, unplanned generation outages and a prior year benefit from insurance proceeds.

We experienced mild weather in our jurisdiction with $0.14 of unfavorable EPS year-to-date compared to the same period last year. Compared to normal, weather was $0.11 unfavorable. As natural gas commodity prices moderated and became more stable in 2024, we recognized a mark-to-market benefit of $0.03 per share year-to-date year-over-year.

Moving to O&M. I'm extremely pleased with our team's success in managing our expenses below our projected 3.5% year-over-year increase to mitigate mild weather, unplanned generation outages and rising insurance costs. O&M increased $0.10 or 1.8% year-to-date compared to the same period last year.

O&M expense benefited EPS by $0.09 per share, which was offset by $0.05 from unplanned generation outage expenses and $0.14 of prior year benefits related to gains on sales of assets and land. Throughout the year, we have prudently managed expenses and expect our annual O&M cost increase in 2024 to be no more than 2.5% over 2023.

Financing costs included a $0.10 impact from new shares issued and $0.07 of interest expense, driven by higher interest rates. Depreciation and amortization expense drove $0.12 of increase due to new assets placed in service. Income tax was higher due to a prior year benefit from a Nebraska state income tax rate decrease.

In summary, excluding prior year one-time events, our strong margin growth and prudent O&M expense management more than offset mild weather, lower off-system sales, unplanned generation outages and financing and depreciation costs incurred for the growth investments to serve our customers' energy needs.

Our strategic execution is delivering recurring earnings growth, excluding prior one-time benefits of $0.32 per share, year-to-date EPS grew 4% compared to the same period last year. Further details on year-over-year changes can be found in our earnings release and 10-Q to be filed with the SEC later today.

Turning to Slide 10, which depicts our solid financial position through the lens of credit quality, capital structure and liquidity. We continue to reduce our net debt to total capitalization ratio and improve other key credit metrics and our commitment to maintain our BBB+ credit quality target.

During the quarter, we issued $109 million of new equity under our at-the-market equity program which included a block equity trade. As a result, we have issued a total of $182 million year-to-date, which is within our planned equity issuance range of $170 million to $190 million for 2024. Our liquidity remained strong at quarter end with $729 million of availability under our revolving credit facility.

We repaid our $600 million notes that matured in August, and we are evaluating timing and options for refinancing our next maturity of $300 million in early 2026.

Slide 11 illustrates our industry-leading dividend track record of 54 consecutive years. We anticipate growing our dividend at a rate comparable to earnings growth, a dependable and increasing dividend is an important component of our strategy for delivering long-term value for our shareholders. I will now turn the call over to Marne for our business update.

Marne Jones^ Thank you, Kimberly. And good morning, everyone.

I'll start my comments on Slide 13. As Linn mentioned, we continue to demonstrate our strong culture of operational excellence during the third quarter. We upheld our reputation for industry-leading electric reliability as reflected recently by EEI with all three of our electric utilities in the top quartile of reliability for the three-year average through 2023. While reliability is critically important to our customers, it also supports our growing data center demand.

During the quarter, we also advanced our plans for new generation resources to serve growth and meet our Colorado Clean Energy plan requirements, all while maintaining strong reliability and enhancing our resiliency.

I'm also proud to share that last week, the U.S. Department of Labor awarded Black Hills with the HIRE Vets Medallion award for the fifth consecutive year. This award recognizes organizations with exemplary efforts in recruiting, employing and retaining our nation's veterans. We value our veteran colleagues and the dedication and leadership they bring to our team and culture.

On Slide 14, I'll provide a status update on our rate reviews. We continued to reach constructive results during the quarter. In Arkansas, we received approval for new rates effective in October. The approved settlement allowed $25.4 million of new annual revenue which includes a return on equity of 9.85% based on 46% equity.

In Iowa, we reached a settlement for our rate review request. Pending approval by the Iowa Utility Commission, the confidential settlement allows $15 million of new annual revenue based on a 7.21% weighted average cost of capital. The settlement provides for implementation of final rates in the first quarter of 2025 and which will replace the interim rates.

Our other active rate review is for Colorado Electric. We received answer testimony from the interveners in October, and we will respond with rebuttal testimony due later this week. Our hearing on this docket is scheduled for December.

Slide 15 outlines our wildfire management and risk mitigation plans. We have been successful in reducing risk with our multilayered approach through asset programs, integrity programs and operational response, which is detailed in our wildfire mitigation plan available on our website.(www.blackhillsenergy.com/wildfire-safety)

We continue to engage stakeholders including community and local agencies regulators, legislative bodies and our industry peers to define, review and advance our wildfire management and mitigation plans, including our Public Safety Power Shutoff program, or PSPS, which we expect to formalize in the first half of 2025.

Moving on to Slide 16. Our largest active capital project is our Ready Wyoming transmission project. The 260-mile line is being constructed on schedule, and we are tracking to place in service our first segments later this year. The project is expected to be completed by year-end 2025. The investment for this project will be recovered through our Wyoming transmission rider as segments are placed in service.

Slide 17 provides an update on our Colorado Clean Energy Plan. Yesterday the Colorado Commission deliberated and verbally authorized 100 megawatts of utility-owned solar, 50 megawatts of utility-owned battery storage and a 200-megawatt solar PPA. With the recent deliberations, we expect a final written commission decision before year-end, and we expect to initiate contract negotiations with the selected counterparties following the written decision.

Slide 18 outlines our South Dakota Electric resource plan. We continue to pursue 100 megawatts of utility-owned generation that will cost effectively and reliably serve our customers. We are targeting an in-service date in the second half of 2026 for 100 megawatts of dispatchable natural gas-fired generation.

We filed a pre-application with the South Dakota PUC during the third quarter and plan to request a certificate of public convenience and necessity from the Wyoming PSC and a permit to construct from the South Dakota PUC and early 2025. With that, I will turn the call back over to Linn.

Linn Evans^ Thank you, Marne. Once again our team made strong progress on our strategic initiatives as we invest in safe, reliable and resilient energy delivery for our customers. We continue to execute our regulatory plan and aggressively pursue our strategic growth opportunities including serving data center and blockchain load growth.

Finally, I want to express my sincere appreciation to the Black Hills team for effectively and efficiently serving our customers while managing through unexpected challenges of the year. With that, we'll be happy to take your questions.

QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) Our first question comes from Andrew Weisel with Scotiabank.

Andrew Weisel^ My first question is you mentioned the unplanned outages a couple of times there. Can you give a little more detail on what exactly were the issues? And what was the O&M impact to earnings?

Marne Jones^ Andrew, this is Marne and thanks for the question. I'll get us kicked off, and I'll let Kimberly jump in on the financial side of it. So this quarter, we had a rollover. Last quarter, we announced that we had a couple of outages driven by some components that failed. One of those outages just rolled over into the early part of Q3. And so that was the impact. There was no additional outages this quarter. I'll turn it over to Kimberly from the financial impact side of it.

Kimberly Nooney^ Yes. Are you asking for the quarter or for the year, Andrew? Andrew Weisel Both if you can share that.

Kimberly Nooney^ Yes. They're on the slides that you can look at, I believe it's $0.03 and $0.05, respectively. But when you look at it in total, you include the impact from the margin side as well. So if you look at the slides, you can see the collective both from the margin impact and the O&M impact from the implanted outages. Hopefully, that will get you what you need.

Andrew Weisel^ Perfect. Yes. Great. I appreciate that. Then along those lines, I believe you're reiterating the guidance for the year. You mentioned those negatives, and you're mitigating that with some better-than-expected O&M trends. Are you able to comment where within the range you might be trending high, middle or low end?

Kimberly Nooney^ Great question, Andrew. No. We don't comment on where we're at in the range. just the fact that we have reaffirmed the range and we expect to achieve the financial objectives that we've laid out for the year.

Andrew Weisel^ Okay. Fair enough. Next is a high-level question, and I realize it's only been a little more than 24 hours since we've known the election results, but you guys are very well positioned in terms of crypto and bitcoin and blockchain and all that. Obviously President-elect Trump has made it clear that he supports those industries, and we've seen a huge spike in the price of crypto. Any early level thoughts on what the incoming administration might mean for that industry and how you and your service territory might be uniquely positioned to benefit.

Linn Evans^ Andrew, this is Linn. Thank you for that question. We appreciate it. I'd like to -- I guess I like our strategy because it's really focused on our customers and what's best for our customers with respect to how we help them grow -- serve their energy needs.

So we're -- I would say we're fairly agnostic to what federal policy might be in that regard. However, our states certainly have a lot of say in our policy and how we serve our customers. That's where we tend to focus the most. But I think your sentiment is indeed right and correct. We've been serving data centers for more than a decade. We're particularly good at it. And we think that, yes, it could have a benefit for us going forward, or we know it will for having going forward.

Andrew Weisel^ Okay. You said data centers. I think you meant these other customers, though, right?

Linn Evans^ I did. It's just in general, we treat them all largely the same. We have different tariffs for each one, but we understand that reliability is critical to them. The service quality that we provide them is critical, et cetera. So we kind of serve them all kind of the same way if you will, but obviously different forms of tariffs and things of that nature.

Andrew Weisel^ That makes a lot of sense, thank you

Operator^ Our next question comes from Chris Ellinghaus with SWS.

Christopher Ellinghaus^ Linn, you've sort of persistently talked about the upside from the large load customers. Is there any kind of cadence to what you're expecting? Are there particular years you're expecting new loads? Can you give us any sort of insights on that?

Linn Evans^ Yes. Thank you, Chris, for that question. The beauty of having served one of our, what I'll call our anchor tenants for over a decade is we understand their cadence, they inform us where they're headed and they meet those measurements just kind of lockstep. So that goes very well for us. It's actually kind of relatively smooth with the data center we're serving currently.

We announced Meta last quarter. They come on the end of 2026. So that will be -- they'll come on kind of gradually as well. So I think that's the beauty, frankly, of these calls that the data centers that we're serving is that they come on and then they have a cadence as they grow and as they expand. I can say -- I can tell you that they have bought land around Cheyenne, et cetera. So we see expansion going on for some time.

Christopher Ellinghaus^ Are you seeing any sort of acceleration given the investment in AI computing at this point?

Linn Evans^ I don't know if we've seen acceleration. We've seen stronger interest in terms of the inbound calls that we take. And historically, for us, Cheyenne has been such a great place for data centers, and still is, because of the fiber optic network that is very rich in the Cheyenne region. And my understanding is with the AI, there's less fiber dependent.

So we're actually encouraged by the possibility of having data centers and particularly AI centers in other parts of our service territory and then bringing our skill set that we've gained over the last decade, we think that can give us some advantage.

Christopher Ellinghaus^ The new intertie also factor into that?

Linn Evans^ Didn't quite understand the new -- the ACDC tie, I'm sorry?

Christopher Ellinghaus^ Yes. Are there reliability thinking?

Linn Evans^ It certainly impacts our reliability thinking. It always does for any kind of a customer, yes. It gives us some flexibility to take energy back and forth across to two separate grids. The grid boundary is right here at Rapid City. So we're accustomed to that to know how to deal with that.

Christopher Ellinghaus^ Okay. The upside to the CapEx slide -- have you got any color that you want to add to that in terms of the types of investments that you're thinking about?

Linn Evans^ The types of investments tend to be right down the center of the fairway for us to use the golf analogy transmission on both electric and gas side. We have perhaps some gas storage opportunities. We've got frankly, more capital projects and maybe you could argue that our customers could afford. So it's always a balance of what's best for customer, what allows us to serve them effectively that costs us effectively and then make sure we generate that return for the shareholder.

Christopher Ellinghaus^ Okay. And Kimberly, can I ask the guidance question a little differently? Given the third quarter results and where the range is sort of suggests a pretty strong fourth quarter. Can you address any of the sort of bigger issues that you are expecting to drive the fourth quarter? And is that O&M number for the year, part of that factor?

Kimberly Nooney^ Yes. So when you think about our full year, you look back at Q1 and Q2, our O&M was actually favorable comparative to the prior year quarters. So we've been managing O&M. Our year started out with pretty mild weather and that's continued. So that's really how we're focused on managing O&M to cover unplanned outages, address some of the insurance expense increases that we've experienced. And so as you look forward, we're really trying to manage that O&M as we started the year, it was about a 3.5% year-over-year increase that we planned for.

But with some of these, what I'd call unexpected challenges with weather, insurance, et cetera, that's really how we're focused on managing it right now as well as making sure we're really diligent on how we think about our capital investments -- I'm sorry, capital investments on behalf of our customers. So I think the guidance that we've given you here should help you achieve how we're thinking about that 4% to 6% growth and how we're thinking about earnings guidance for the year.

Linn Evans^ And Chris, this is Linn. I could not be more proud of how our team has stepped up an incredible way very laser-focused on how we control costs on behalf of customers and then provide the shareholders that return as well. So I just want to take a moment to say a big shout out to our team and how focused they've been and how helpful they've been this past year and going into the fourth quarter.

Christopher Ellinghaus^ I don't recall who -- it was probably Marne, I'm not sure. Somebody mentioned that you took advantage of the outages to do some longer-term maintenance. Does that have an effect on, say 2025? Or what period was some of that maintenance O&M drawing forward from?

Marne Jones^ Yes. This is Marne. So when we do have these larger outages where we're opening up more of the machine, it's an opportunity to pull forward some of that maintenance. Typically, you're looking out one to two years of pulling that forward. It's really dependent on what we find when we open that up.

Operator^ (Operator Instructions) Our next question comes from Julien Dumoulin-Smith with Jefferies.

Brian Russo^ It's Brian Russo on for Julien. Is there any opportunity given your commentary around these data center growth, the 5% of current EPS contribution growing to 10% by 2028? Is that really just the anchor tenant? And also the meta project announced a month or two ago? Or is there more projects that are driving that now?

Kimberly Nooney^ Yes, Brian, this is Kimberly. A couple of comments there. I would generally say it's an anchor tenant. It includes Microsoft and meta. But as Marne mentioned, those, and Linn mentioned, those data center loads continue to evolve over time.

Linn mentioned the land that they're purchasing. So there are future opportunities. But at this point, we're focused on that 5% to 10% growth. We obviously work with both meta and Microsoft to evaluate what their forecasts are, and we will be updating that as we go into Q4 and announce all of our capital and earnings guidance in February.

The one other thing I'd note is we are getting additional inbounds not just in Wyoming including conversations that we're having both in Colorado and South Dakota. So that will also inform our future EPS growth as we continue to partner with potential other data centers in our territory.

Brian Russo^ Yes. That was actually going to be my next question outside of Wyoming. A lot of these customers you mentioned are very active in the Dakotas and Colorado as well. Will you look to set up some sort of a similar kind of LPCS (Large Power Contract Service) or BCIS (Blockchain Interruptible Service) tariff structure that these customers are receptive to that in Wyoming in these other states.

Linn Evans^ Brian, this is Linn. Thanks for that question. I'd say the answer is maybe, we pride ourselves in doing what we think is really good for customers and shareholders. So we'll be flexible.

We have lots of different -- we have multiple tariffs that we could use, multiple avenues that we can serve them. And for us, because of our size and our ability to be agile, we can modify and do what we think is -- does well for the customer but making sure we also protect the shareholder. So that's my approach to that.

Operator^ Thank you. I would now like to turn the call back over to Linn Evans for any closing remarks.

Linn Evans^ Well good morning again. Thank you for joining us today and especially thank you for your interest in Black Hills. We'll be seeing a number of you starting this weekend at EEI, so please travel safe.

We look forward to engaging with you there. Once again I want to say a sincere thank you to the Black Hills team. I just really appreciate how all of us has stepped up this year to make sure we serve our customers and our shareholders excellently. And you've done that. So thank you so much. I encourage everybody to have a Black Hills Energy safe day. Take care.

Operator^ Thank you. This concludes the conference. Thank you for your participation. You may now disconnect.