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PRESENTATION

Operator

Good day, ladies and gentleman. This is your conference operator. At this time, I would like to welcome everyone to the Q1 2019 Evergy Inc. Earnings Conference Call. (Operator Instructions) Thank you. I would now like to turn the call over to Lori Wright, you may begin your conference.

Lori A. Wright - Evergy, Inc. - VP of Corporate Planning, IR & Treasurer

Thank you, Lori. Good morning, everyone, and welcome to Evergy's first quarter call. Thank you for joining this morning. Today's discussion will include forward-looking information. Slide 2 and the disclosure in our SEC filings containing a list of some of the factors that could cause future results to differ materially from our expectations and includes additional information on non-GAAP financial measures. We issued our first quarter 2019 earnings release and 10-Q after market close yesterday. These items are available, along with today's webcast slides and supplemental financial information for the quarter, on the main page of our website at evergyinc.com.

On the call today, we have Terry Bassham, President and Chief Executive Officer; and Tony Somma, Executive Vice President and Chief Financial Officer. Other members of management are with us and will be available during the question-and-answer portion of the call. As summarized on Slide 3, Terry will recap the quarter and provide a business update. Tony will update you on the details of our latest financial results.

With that, I'll hand the call to Terry.

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Thanks, Lori, and good morning, everybody. I'll begin on Slide 5. 2019 is an important year for our company. We're targeting strong year-over-year earnings growth as we capture the benefits of the merger. Last night, we reported first quarter GAAP earnings of $0.39 per share compared to $0.42 per share earned in the first quarter of 2018. Adjusted earnings were $0.44 per share in first quarter 2019 compared to $0.34 in the same period a year ago. The year-over-year increase in earnings was primarily driven by cost-reduction efforts and higher retail sales due to colder weather.

I'm pleased with the execution of our team and we saw the first quarter delivered, which keeps us on pace to achieve our 2019 targets. As we focused on our plan, cost reductions and share repurchases, mother nature presented us with a few challenges during the quarter.

As we previously stated, our team banded together to restore power during a major storm that hit Kansas City in January, which was a once in a couple of decades kind of storm. At its peak, we had about 200,000 customers out of service. But through the dedicated work ethic of our team, we fully restored customers within 5 days of the event. Separate from the January storm, we also had flooding that impacted our service territory in March. The latan generation station near Western Missouri was our most at risk piece of infrastructure. If you recall, in 2011, we experienced flooding in the same region. One silver lining of dealing with the 2011 event, we've been more prepared for conditions as they developed this year. Emergency plans and infrastructure builds 8 years ago allowed us to withstand the floodwaters without a significant impact. We did alter our day-to-day operations for about a 1.5 weeks, but we're able to resume normal operations by the end of March. I'd like to give a special praise to our folks in the field that worked in less than ideal situations that you might imagine to ensure the protection of our assets and keep customers' power interruptions to a minimum during these events.

Before I move on, let me update you on our efforts towards renewable energy, mainly affordable wind. Kansas now ranks #1 with respect to wind resources as a percentage of megawatt hours produced. Our company recently reached a milestone by producing over 50 million-megawatt hours of wind. To put that in perspective, that's enough power to light up Times Square for more than 3 decades. Locally, we have been working with the City of Kansas City, Missouri, to achieve their goal of offsetting 100% of their municipal electric energy usage with energy produced from carbon-free sources by 2020.

We continue to see more and more demand for our existing -- from our existing customers and potential new customers to be supplied with the abundant renewable resources found within the states we serve.

Now moving on to Slide 6. I'll give you the latest on our regulatory and legislative proceedings. As you may recall, we agreed to produce the Kansas rate study as part of our merger agreement last year. We completed the study and presented the results to the House of Senate early in the Kansas legislative session this year. The KCC staff also completed similar, but yet separate study of Kansas rates to present their findings to the legislature as well. Throughout the session, Kansas rates continue to be a topic of discussion. Ultimately, Senate Bill 69 was passed, sign into law by Governor Kelly in April and authorized an independent retail rate study of Kansas Electric Public Utilities. The study will provide information that may assist future efforts of developing electric policy aimed at delivering regional, competitive rates and reliable electric service.

The process is expected to take place throughout the remainder of this year with findings to be delivered starting in January of next year. Let me be clear, we believe the merger, with its upfront and ongoing bill credits and significant cost efficiencies, has tremendous benefits for our customers prices for years to come and goes a long way toward addressing these concerns.

In March, Governor Laura Kelly appoints Susan Duffy to the Kansas Corporation Commission. Commissioner Duffy previously served as Executive Director of KCC staff and most recently as the General Manager of Topeka Metro responsible for the management and operation of the Topeka transit system. We look forward to working with her as she transitions into her new role into KCC.

Now moving to the latest proceedings in Missouri. In March, the Missouri Public Service Commission set a procedural schedule to hear complaint regarding GMO's Sibley plant, which we retired in the fourth quarter of last year. The complaint asked the commission to issue an accounting authority order to defer all costs we avoid that are currently reflected in retail rates, except for depreciation that is associated with the retired generation unit.

Direct testimony was filed in April by the complainants, Office of Public Counsel and an industrial customer group and we'll file our rebuttal testimony later this month. Hearings are set for mid-July and we expect a commission order by early September. Missouri legislative session has been mainly focused on education, workforce development and infrastructure funding. We don't expect any of the energy-related bills to receive the traction needed to move forward this session.

Now turning to Slide 7. Let me update you on the latest regarding our merger plans. Upon launching our merger, we laid out 3 specific priorities we remain keenly focused on: achieving target merger savings, rebalancing the holding company capital structure by repurchasing shares, an attractive EPS dividend growth with reduced risk given our regulatory stay-outs. We have moved the ball in the right direction on each of these objectives.

First, we exceeded our 2018 gross merger savings target. We feel confident in achieving the $110 million target that we set for this year. Next, we laid out our share repurchase strategy with the intent to dollar-cost average over time, while taking a programmatic and opportunistic approach.

We stuck to that plan, while utilizing accelerated share repurchases and open market repurchases being optimistic when it makes sense. The activity in the quarter kept us on track to complete our target share repurchases by the mid next year.

Lastly, on earnings and dividend growth. Our original EPS guidance based on 2016 set the foundation for implied range through 2021. Our 2019 adjusted EPS guidance and our expectations for EPS growth over the next couple of years are consistent with our original implied 2021 range albeit at the middle to lower end. Our currently indicated annualized dividend of $1.90 per share lands us in the middle of our targeted long-term dividend payout ratio of 60% to 70% when applied to the $2.90 midpoint of our 2019 adjusted EPS guidance. Nothing has fundamentally changed since we laid out the original merger plan. We are executing and continue to have confidence in our ability to deliver.

In fact, between dividends and share repurchases, we've committed to distribute $700 million of capital to shareholders in just the first quarter alone.

Now moving to Slide 8, I'll update you on our investment outlook before I turn things over to Tony. With solid first quarter results, we're affirming our 2019 adjusted earnings guidance range of $2.80 to $3 per share. The $2.90 midpoint is the base from which we target our long-term EPS CAGR of 5% to 7% through 2023, which we've indicated is currently forecasted to be nonlinear and front-end loaded. Many of you have asked about growth post 2021, so let me describe how we're approaching the future. As we've said many times over the last couple of years, one of the largest benefits to our plan is the opportunity to keep customer bills low, deliver a safe, reliable product and target competitive shareholder returns. Our unique plan positions us well to achieve these objectives. Minimizing the impacts to customer bills and competitively positioning customer rates is the foundation of our 5-year capital plan.

Our rate base growth projections are by design and set at a forward level to maintain reliability for our customers, build adequate regional transmission infrastructure and include line of sight projects with no placeholders.

Our lower projected CapEx compared to many of our peer positions us uniquely from a cash flow perspective. Again, this is by design and result in projected free cash flow post 2021, even after paying a dividend. This protects against the downside of rate pressure and positions us with flexibility. We expect several levers to be available to us in the latter half of our 5-year plan that will allow us to keep customer bills low and provide opportunity for attractive shareholder returns. Some of those levers include, infrastructure projects that aren't currently on our plan, but might be of benefit for customers in the future. This could include incremental spend, reallocation of our current 5-year plan, $6 billion CapEx or some combination of the 2. We intend to deploy capital investment where it's wanted and reward it as evidenced by the regulatory construct, while balancing the needs of our customers and reliability metrics in the respective jurisdictions.

To that end, we continue to look for opportunities that allow us to further utilize PISA of legislation in Missouri. Or we could look at deleveraging the holding company once we've completed the share repurchases. Now this is an exhaustive list, but does include some of the strategies available as we look out over the next 5 years. We'll continue to focus and remain flexible as we move forward through this transition period. A key reserving the future optionality hinges on our ability to deliver the value of the merger thesis and we are on track to deliver on our commitments.

So with that, I'll turn the call over to Tony.

Anthony D. Somma - Evergy, Inc. - Executive VP & CFO

Thanks, Terry. Good morning, everyone. I'll start with results on Slide 10 of the presentation. Last night, we reported first quarter GAAP earnings of $100 million or $0.39 per share compared to $61 million or $0.42 per share in the first quarter of '18. The increase in earnings is primarily due to the inclusion of KCPL's and GMO's results in the first quarter of 2019, which aren't included in Evergy's first quarter 2018 results.

GAAP EPS was $0.03 lower, primarily due to the dilution of shares issued to Great Plains Energy shareholders upon closing of the merger. Adjusted non-GAAP earnings were $111 million or $0.44 per share compared to $92 million or $0.34 per share in the same period a year ago. As detailed on the slide, adjusted EPS was up $0.10, primarily driven by cost reduction efforts, peer shares outstanding and colder than normal weather. Some additional drivers for the quarter include gross margin being up $22 million, primarily due to new retail rates, net of the 2018 provision for rate refund for the lower corporate tax rate, and favorable weather, which we estimate contributed about $0.05 compared to first quarter 2018.

O&M was down $30 million primarily driven by cost reduction efforts associated with merger-enabled efficiencies and plant retirements in Missouri. Depreciation and amortization was $30 million higher, primarily from new depreciation rates that are reflected in our retail prices.

And lastly, accretion resulting from share repurchase activity which added about $0.03 a share.

For the quarter, pro forma residential sales were up 4.5% and commercial sales were up 1.7%, primarily due to the colder weather, which we estimate helped about $0.06 when compared to normal. Pro forma industrial sales were about 3.5% lower in the same period last year. Most of this decrease comes from a large customer in the chemical sector that saw decreased demand at their plant in our service territory.

From an economic standpoint, things have stayed steady in our territories. Unemployment rates continue to hover in the low to mid-3% range, remaining below the national average. We saw a nice pickup in multi-family home construction, marking the highest quarterly numbers in this area in the last couple of years. Steady growth remains present in the business services, health care and pet sectors. A pet technology company recently announced the relocation of their headquarters from Silicon Valley to Kansas City. This should bring a few hundred jobs and add to the established animal science corridor that is present within our territory.

Now moving on to Slide 11. Let me touch on our latest financing activities. In March, we issued $400 million of KCPL bonds at 4.125%, replacing bonds with a coupon of 7.15%. As far as upcoming maturities, KG&E has $300 million of first mortgage bonds coming due in June that we'll look to replace.

Moving on to the holding company. In March, we entered a $1 billion term loan that will expire in September. This allows us to continue our share repurchases between now and later this year, where we project to issue about $1.5 billion of long-term holding company debt. While repurchasing 60 million shares by the next year continue to be our target, the ultimate amount of holding company debt needed will vary based on share price timing and total number of share repurchases. All of which are subject to market factors and the financial outlook of the company.

Throughout the first quarter, we repurchased over 10 million shares through the combination of ASRs and open market purchases. As of the end of April, we've now purchased around 46% of the total 60 million shares -- share target, and we'll still have outstanding in ASR that has not closed.

Wrapping up on Slide 12, as Terry mentioned, our first quarter results started the year in a right direction, so we are reaffirming our 2019 adjusted EPS guidance range of $2.80 to $3 per share. We remain focused on delivering significant cost reductions, while executing our investment plan that minimizes lag during our regulatory stay-out period over the next 4 to 5 years.

Again, to echo what Terry said, we're being very intentional with our capital allocation, giving preference to earning certainty, zeroed on earning our allowed returns and maintaining flexibility for the future and returning capital to you, our shareholders. We remain confident in the plan that we've laid out and continue to believe our thesis offers a competitive and attractive risk-adjusted total shareholder return profile, while focused on keeping customer rates competitive.

With that, I'll turn the call back over to Terry.

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

All right. Thank you for joining us. We'll take questions now.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Greg Gordon from Evercore ISI.

Gregory Harmon Gordon - Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Power & Utilities Research

A couple questions. First, am I right that when you called out that the storm costs, all things equal, had a $13 million impact in the quarter. So despite that, it's like almost $0.05 headwind, you still were able to get to the $0.44 number?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

That's correct.

Gregory Harmon Gordon - Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Power & Utilities Research

Okay. And that when you look at what average annual storm costs look like in a normal year, would you expect that, that would be something that might recur normally year-over-year, but just happened over the course of time? Or do you see that as an exceptional event?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

No, that was an exceptional event, that's why I mentioned it's a -- I guess, we say it a lot now, couple in the decades event, but, no, we normally don't have that many customers out 5 days. And so not only do you have extra expense, but you got lost revenue. So that is not normal and haven't -- in fact, I've been here almost 15 years and it's the worst storm we've seen since I've been here.

Gregory Harmon Gordon - Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Power & Utilities Research

Well, congratulations on getting your customers back so quickly. My second question goes to your capital allocation commentary. And I know that customer affordability is a huge issue for you and you are rightfully primarily focused on it and it's one of the reasons for the merger. And so you've been very careful about not trying to send the wrong message to our customers about capital spending, but at the same time, I'm hearing you talk about an increased desire for renewable energy from your customers. One of the things that I'm also seeing industry-wide is the ability to deploy new technologies that while they do increase capital spend also improve the customer experience and potentially lower bills, so as you think about the back-end of that CapEx program in '22 or '23, not to put words in your mouth and disguise a question as a statement, but are those the type of things that are not yet in the plan that you're thinking about? And can you elaborate perhaps on that?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Yes, you're exactly right. Obviously, focused on, as you said, the near-term stability after each company spent 10 years on both reliability, generation and environmental spend. This period post-merger with the synergy savings provide an opportunity for growth is critical. But as you described also, we have ever-changing needs from what customers want and we are very fortunate to have the opportunity to be near one of the best wind resources in the country. We see that as not only an ability to serve our current customers, we see that as an ability to attract economic development from new customers. And we are part of our teams in each of our states and each of our cities. When we talk to folks considering moving to a region about that opportunity, what used to be a green opportunity is now also a green and a low cost opportunity given the technologies around that. In addition to that, you're exactly right, we also have both reliability and customer desire technologies that we're dealing with every single day like everybody is. And that's an area where PISA in particular provides us with a great opportunity to ramp up spend in a way that's structured and approved in Missouri and almost expected. So we're looking at the timing and the ability to do those as well. So each one of those gives us the ability not only to be stable in the short term, but provide for that additional growth in the long-term, and we look forward to updating shareholders along the way as we finalize some of those plans.

Gregory Harmon Gordon - Evercore ISI Institutional Equities, Research Division - Senior MD and Head of Power & Utilities Research

Congratulations on a good quarter.

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Thank you very much.

Operator

Your next question comes from the line of Ali Agha from SunTrust.

Ali Agha - SunTrust Robinson Humphrey, Inc., Research Division - MD

First question, Terry. So the Kansas rate review that would finish up in early 2020, to the extent that define the rates are too high for whatever reason, how would that actually impact you guys given that you have a rate freeze as part of your merger agreement, I'm just thinking about the logistics here, if there is some negative ruling that comes out there?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Yes, I mean, I don't know for sure. What I would tell you is that we are very confident that this is the legislature, which would look at opportunities maybe to send to the commission, further work to be done, potentially. But we certainly see that the ultimate outcome of the study should reflect not only the current benchmarking, if you will, with our rates, but the historical development of our cost and rates and what we see in the future, which again, is consistent with what we just talked with Greg about and that's what our current merger opportunity provides us with, assurances to those legislators that we see the same issue and have addressed it and our merger does just that. Process-wise, we saw some legislation this time that we didn't think really was appropriate. And obviously, the legislature agreed that we got to be talking about a study before we look into those kind of things. But certainly, if they have particular concerns, we're confident that we'll be able to work with our legislators and our local customers about options that may help solve those problems in a way that makes sense both to them and to our shareholders.

Ali Agha - SunTrust Robinson Humphrey, Inc., Research Division - MD

And generally speaking, are you and the staff on the same page on this? Or is staff in their study thinking differently?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

No, we actually presented our own study side-by-side. Our witness and their witness and answered the same questions and we are locked step. I would say that our relationship through the (inaudible) merger too, where we worked through the final merger settlement in the process for the structure of that stay-out and overview, put those in a position of absolutely being consistent in our voice through our legislators.

Ali Agha - SunTrust Robinson Humphrey, Inc., Research Division - MD

Okay. Second question, just clarifying your comments from earlier. So as you mentioned -- you're fairly confident in the earnings growth that you've laid out for us through 2023, which by definition implies that the growth in that '21 through '23 period of roughly 5%-or-so is exceeding what your current rate base growth would be from the current CapEx plan, which is in the 2% to 3% range. So it appears that you run the math and you've identified potentially the levers already that would keep you in that growth trajectory. A, is that right in terms of potentially the CapEx that you could incrementally spend? And b, when would you convey that to us and the investment community in terms of what kind of opportunities you see for potential increase in CapEx in those outer years?

Anthony D. Somma - Evergy, Inc. - Executive VP & CFO

This is Tony. So there is near various obviously levers that come up with our guidance range, especially, particularly, when you're going out that far to 2023. Some of them we mentioned in the script which is we could potentially delever the holding company. We can look at increasing on our spend if it's right for our customers and for our shareholders where we don't have a lot of regulatory lag. And so as we look at things going out and that we'll gain more certainty throughout the planning year this year and we would hope to maybe to the extent the stuff changes, we would let folks know either foreshadow that at EEI and needing more clarity with some of the numbers when we do our year-end 2019 call.

Ali Agha - SunTrust Robinson Humphrey, Inc., Research Division - MD

I see. And last question just clarifying the 46% roughly of the share buyback, total buyback that you completed. Does that include the ASR that was announced, but not completed? Or is that not that factored into this?

Anthony D. Somma - Evergy, Inc. - Executive VP & CFO

It includes the initial delivery of some shares, but ASR is not closed. And so the parties will give us the remaining shares when the contract terminates.

Ali Agha - SunTrust Robinson Humphrey, Inc., Research Division - MD

So putting all of that, how much is bought back?

Anthony D. Somma - Evergy, Inc. - Executive VP & CFO

Well, as of the end of the April, it's roughly 46%, almost 27 million shares.

Operator

And we have a question from the line of Michael Sullivan from Wolfe Research.

Michael P. Sullivan - Wolfe Research, LLC - Research Analyst

I just -- I first wanted to just touch on Kansas. Now that we've sort of gotten through this legislative session and seen the bill that ultimately got passed, but some of the other things that were discussed, could you guys just give us a sense or are you feeling better or worse about the whole political dynamic there, as we go into next year and we get the rate study results and you have a new legislative session. Just your thoughts there?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Yes, we are feeling better actually. Certainly, when initial bill got passed or filed, our initial bills got entered, we became a topic of conversation. And so other folks who had concerns, some of them related to, for example, demand on renew -- on a solar installation. So things that were kind of out there, but just we became part of the discussion. I would say that through that we've talked to folks and solved many problems that were kind of one-offs or specific issues, I'd say. And the study to be conducted now with everybody in the room together, it gives us the ability to have those conversations along the way and not necessarily have as much debate at the very end after we completed. So I think our ability to continue to talk to people over the next 12 months, our ability to work with an independent consultant and our customers that evaluate all the concerns and issues is actually a positive from an outcome starting in January next year.

Anthony D. Somma - Evergy, Inc. - Executive VP & CFO

And I'll add, we're continuing to give back merger credits to the tune of $11.5 million a year in Kansas.

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Yes. it's a good point. We remember, we gave our first credit back in the first year after all that was going on. By the time we get to the end of the year, don't know whether we have seen that, but know what's in front on this as well. So it will affect those acknowledgments of what the merger means to our customers.

Michael P. Sullivan - Wolfe Research, LLC - Research Analyst

Great. And then just, Terry, on your comments on Slide 8 on the whole capital plan and what that looks like further out in time. Could you just be a little more specific on reallocation versus incremental? And what is going to drive that? And when we will have a better sense of sort of how that plays out?

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Yes. Tony kind of covered it, but what I would say is if you just looked at percentage allocations by state, remember that it's in part an allocation based on the number of customers in that state. So it may look like it's a little heavier one direction than other, but that's based on population. But more importantly, the commitment around the merger, in particular, in Kansas, provide stability, but also provides consistency, whereas the PISA bill in Missouri is specifically geared toward additional spending around infrastructure. We've seen Ameren go out with a plan and seeing what they're doing and have gotten very good responses from the commission. So we see an opportunity there to be able to potentially allocate more in that direction under the PISA structure, which doesn't exist in Kansas. And then, as you go along, you'll continue to see projects that are very specific. We've talked about the fact, we didn't put kind of general buckets out there, but as we develop projects, there may be more projects related to 1 need or another in a state, it's very specific. So as we work through those allocations and budget plans, especially in that back-end period, you could see a focus on 1 jurisdiction versus another. I will remind you that Missouri is still in a position where we have some lag there. We overspend absent PISA, but they are also looking at shortening the time period for rate cases over there. So if that were to continue to develop, that might give us additional opportunity without creating lag before we got to the end of the period.

Michael P. Sullivan - Wolfe Research, LLC - Research Analyst

Okay. Great. And then just 1 last one, on 2019, I just wanted to clarify. I think when you gave guidance for the year on the last call that already baked in those storm costs, but then weather was actually $0.06 better than normal, I think, Tony said. Was that baked in as well? Or would that be favorable to what you guys were seeing at the time?

Anthony D. Somma - Evergy, Inc. - Executive VP & CFO

So this is Tony. We -- when we come out with our -- came out with our guidance and our drivers to get to the $2.80 to $3 a share, it will be assuming normal weather.

Operator

Your next question comes from the line of Charles Fishman from MorningStar Research.

Charles J. Fishman - Morningstar Inc., Research Division - Equity Analyst

I just want to make sure I got this right. Okay, you are reaffirming the 5% to 7% with the base of $2.90 for this year. But did I hear that the EPS growth will be a little above, maybe the higher end of that range in the early years and lag in the later years unless some potential CapEx comes along? Or were you just referring to the merger savings being front-end loaded, which are obvious from the information you provided? If you can just clarify that for me, I'd appreciate it.

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Yes, well, they are both correct. I mean obviously, on the front end, as we ramp up the savings, there is an early lumpiness, if you will, trending on the front-end that drives in part the EPS pathway as well. And again, as it does that, the back-end is a little softer, we are talking about what we're doing to look at opportunities and needs for additional spending on the back-end from that perspective.

Operator

And there are no further questions at this time. I'll turn the call back to Terry.

Terry D. Bassham - Evergy, Inc. - President, CEO & Director

Thank you, Lori, and thank you everybody for calling in this morning. Off to a good start and look forward to talking to you throughout the year. Thank you very much. Have a good day.

Operator

This concludes today's conference call. Thank you everyone for your participation. You may now disconnect.
