

CMS Energy Corporation NYSE:CMS

FQ1 2023 Earnings Call Transcripts

Thursday, April 27, 2023 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2023-			-FQ2 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.70	0.70	●0.00	0.68	3.10	3.34
Revenue (mm)	2321.38	2284.00	▼ (1.61 %)	1923.39	8623.34	9041.30

Currency: USD

Consensus as of Apr-24-2023 7:27 PM GMT

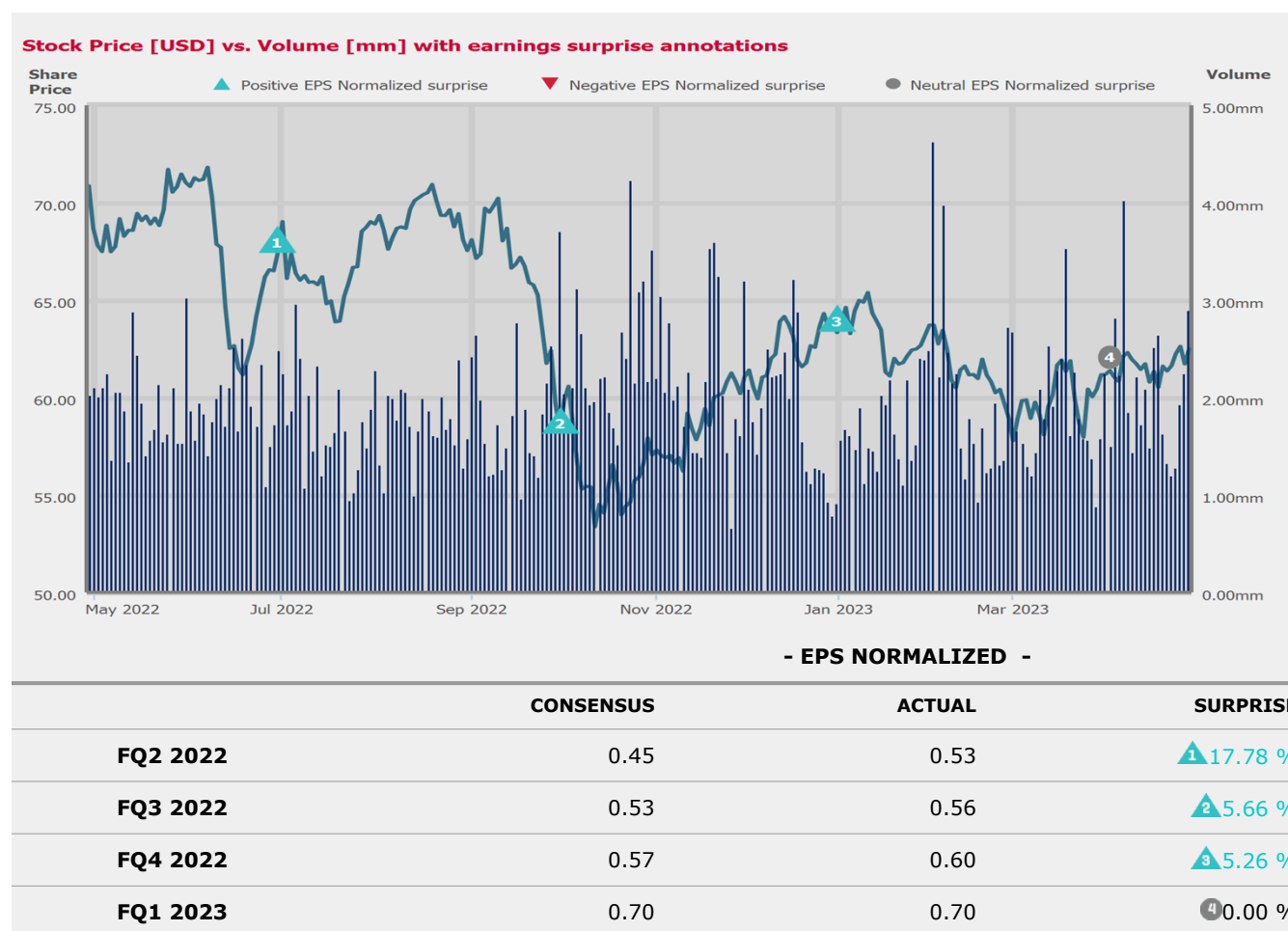


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Call Participants

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Presentation

Operator

Good morning, everyone and welcome to the CMS Energy 2023 First Quarter Results. The earnings news release issued earlier today and the presentation used in this webcast are available on the CMS Energy's website in the Investor Relations section. This call is being recorded. [Operator Instructions]

Just a reminder, there will be a rebroadcast of this conference call today beginning at 12:00 p.m. Eastern Time running through May 4. This presentation is also being webcast and is available on CMS Energy's website in the Investor Relations section.

At this time, I would like to turn the call over to Mr. Sri Maddipati, Treasurer and Vice President of Finance and Investor Relations.

Srikanth Maddipati

VP of IR & Finance and Treasurer

Thank you, Bailey. Good morning, everyone and thank you for joining us today.

With me are Garrick Rochow, President and Chief Executive Officer; and Rejji Hayes, Executive Vice President and Chief Financial Officer.

This presentation contains forward-looking statements, which are subject to risks and uncertainties. Please refer to our SEC filings for more information regarding the risks and other factors that could cause our actual results to differ materially. This presentation also includes non-GAAP measures. Reconciliations of these measures to the most directly comparable GAAP measures are included in the appendix and posted on our website.

Now I'll turn the call over to Garrick.

Garrick J. Rochow

President, CEO & Director

Thank you, Sri and thank you, everyone, for joining us today. Our commitment to industry-leading financial performance spans 2 decades and it's this investment thesis that is foundational to our performance. Over that time, we've experienced changes in commissions, legislatures and governors, unplanned weather and storms, recessions and a pandemic. In each and every year, we have delivered for our customers and for you, our investors. It's the -- it's the performance you have come to expect from a premium name like CMS Energy and this year is no different.

We remain squarely focused on our mission at CMS Energy, making the needed investments in safety, reliability and decarbonization of our system, balanced by customer affordability and our \$15.5 billion 5-year customer investment plan. These investments in our expansive and aging electric and gas systems are critical to enhance reliability and resiliency and are supported by Michigan's constructive legislation and regulatory framework.

Our investments are coupled with our lean operating system, the CE Way, which helps us manage and lower cost. This ongoing drive to see and eliminate waste is evident from the field to the office and helps improve our efficiency, ensuring we deliver customer value while keeping bills affordable. We are committed to this. And I believe we do it better than most -- any company in the industry.

As we round out the first quarter of 2023, I want to share a few highlights. First, Ford's announcement of the BlueOval Battery Park. This is another important win, which brings \$3.5 billion, 2,500 jobs and adds to the growing list of economic development projects in our service territory. We saw additional enrollments in our Voluntary Green Pricing program, supporting the build-out of our first large tranche of owned solar representing 309 megawatt of the total 1,000 megawatt approved. Preparations continue for the acquisition and transition of the Covert generating facility scheduled for June as approved by our IRP.

And in our gas business, began construction of our Mid-Michigan pipeline, a \$550 million, 56-mile pipeline to enhance deliverability and safety of our natural gas system.

I want to be clear, at CMS Energy, year after year, regardless of conditions, we are positioned to deliver.

Now let me address the extreme weather we faced in the first quarter. In late February and early March, we experienced the second largest storm event in our service territory. Our line crews are some of the most skilled and experienced in the business. And they showed up with able hands and hearts of service and our customers were well served by their dedication. In addition to our crews in the field, there are hundreds of people behind the scenes to support our crews and our communities, including many of our coworkers, who volunteered to serve customers throughout the restoration.

I know many of my coworkers join our earnings call. And from my heart, I want to say thank you to each and every one of you for showing up for our customers and for each other. Because of our team, working together to serve, 97% of our customers were with power within 3 days.

In our 135-year history, 8 of the most destructive storms have occurred in the last 20 years. That's a significant data point. The severity and frequency of storms we're seeing highlights the need to enhance critical investment and amplify our efforts on the reliability and resiliency of our electric distribution system. We need more undergrounding. This is an area where we are significantly behind some of our Midwest peers. We also need to do more sectionalizing, automated transfer reclosers and looping and overall system hardening. These important investments are critical to improve reliability and resiliency for our customers and will be outlined in our pending electric rate case and in our updated 5-year Electric Distribution Infrastructure Investment Plan.

We also plan to include an investment recovery mechanism in our upcoming rate case to add certainty to our investments. I'm pleased that our commission has been supportive of reliability improvements, doubling our efforts around tree trimming since 2020. This as well as other customer investments has contributed to the 20% improvement in our reliability in 2022. But there is more work to be done and more needed investment. We will continue to work productively with the commission on the reliability and resiliency of our electric distribution system, so we prepare for increasingly severe weather. We expect further alignment and collaboration and the needed investments in the upcoming storm audit as we work on a common goal of improving our distribution system for all customers.

I'm confident in our ability to work with all stakeholders because Michigan has the legislative and regulatory framework in place to enable these investments and to attract the capital needed to drive the changes we all want to see. We have a productive energy law that provides forward-looking test years, constructive ROEs and supportive incentives. It is this environment, which has earned Michigan the rank as a top-tier regulatory jurisdiction for the past decade.

Now I know many of you will want to dive into the details of the back and forth in both the regulatory and legislative arena, which we are happy to do in Q&A, but remember, it's all part of the process. Let me remind you, we have a track record of working with all stakeholders to drive successful outcomes. It's why we settled 3 cases in 2022.

Now I want to be clear where we stand today. We saw both unseasonably warm weather in January and February as well as significant cost with the ice storm. As you would expect, we've taken actions early to counteract that impact. Therefore, we are reaffirming all our financial objectives.

Most importantly, our full year guidance of \$3.06 to \$3.12 per share with continued confidence towards the high end.

In the first quarter, we reported adjusted earnings per share of \$0.70. We're also reaffirming our long-term adjusted earnings growth of 6% to 8% per year with continued confidence toward the high end and remain committed to annual dividend per share growth of 6% to 8%.

This isn't our first rodeo, whether it was the pandemic or weather-related, we managed the work to deliver for both customers and investors through the CE Way and other countermeasures already underway. We

will offset the unplanned headwinds experienced early in the year. I have confidence in our team and in our plan for 2023 and beyond, given our long-standing commitment and performance.

At CMS Energy, we deliver for customers while consistently delivering industry-leading growth.

Now I'll hand it over to Rejji to provide some additional details and insights.

Rejji P. Hayes

Executive VP & CFO

Thank you, Garrick and good morning, everyone.

For the first quarter of 2023, we delivered adjusted net income of \$204 million or \$0.70 per share, largely driven by unfavorable weather and costs related to service restoration as a result of the significant storm activity that Garrick noted earlier. To elaborate on the impact of weather on sales, given the well-publicized warm winter experienced in the Midwest, the number of heating degree days in our service territory during the quarter were approximately 18% below normal weather patterns. The atypically warm weather, coupled with a strong comp in the first quarter 2022 resulted in \$0.27 per share of negative variance versus the comparable period in 2022, as noted on Slide 7.

Rate relief, net of investment-related expenses, resulted in \$0.03 per share of negative variance as last year's constructive electric and gas rate case settlements were offset primarily by the roll off of tax benefits realized in the first quarter of 2022 associated with a prior gas rate case settlement as expected.

From a cost perspective, as mentioned, our financial performance in the first quarter was significantly impacted by higher operating and maintenance or O&M expenses attributable to storm restoration costs, which resulted in \$0.20 per share of negative variance versus the first quarter of 2022. It is worth noting, however, that given the elevated storm costs we've seen over the last few years, we have incorporated fairly conservative assumptions for this cost category in our full year forecast.

Looking ahead, as always, we plan for normal weather, which equates to \$0.14 per share of negative variance versus the comparable period in 2022 due to the absence of strong sales at the electric utility driven by last year's warm summer. We anticipate that the estimated negative variance attributable to weather will be more than offset by rate relief net of investment-related costs, which we have quantified at \$0.17 per share versus the comparable period in 2022. Our underlying assumptions for rate relief are largely driven by last year's successful gas and electric rate case settlements and we have assumed a constructive outcome in our pending gas rate case.

Closing out the glide path for the remainder of the year, as noted during our Q4 call, we anticipate lower overall O&M expense in the utility driven by the usual cost performance fueled by the CE Way. And in light of the weather-related headwinds in the first quarter, we have supplemented our planned productivity for the year by limiting hiring, reducing our use of consultants and contractors, accelerating longer-term IT cost reduction initiatives and eliminating other discretionary spending among other activities. These cost performance measures will support the \$0.28 per share of positive variance versus the comparable period in 2022.

And I'd be remiss if I didn't mention that none of these actions will impact the safety and reliability of our electric and gas business.

Lastly, as we discussed during our fourth quarter call, we're assuming modest growth at NorthStar and the benefits associated with the roughly \$0.12 per share of pull aheads achieved in the fourth quarter 2022 as per our original guide. And to offer further risk mitigation of the financial headwinds encountered in the first quarter and provide additional contingency should we need it, we have supplemented these opportunities with anticipated cost savings at the parent, largely in the form of opportunistic financings and tax planning, which in aggregate, we estimate will drive \$0.36 to \$0.42 per share of positive variance versus the comparable period in 2022.

Before moving on, I'll just note that though our track record of delivering on our financial objectives over the last 2 weeks -- 2 decades speaks for itself, we remain perpetually paranoid in our financial planning

process. More bluntly, we always do the worrying, so you don't have to. And to that end, I'm pleased to report that we've already begun to see the benefit of the numerous countermeasures implemented in the first quarter. As such, I'm highly confident that we will realize the balance of expected savings over the course of the year.

Moving on to the financing plan. Slide 8 offers more specificity on the balance of our planned funding needs in 2023, which are largely limited to debt issuances at the utility, a good portion of which has already been priced and/or funded over the past several months. As we have noted in the past, the parent's contribution of the funding needs of the Covert acquisition is in place with the roughly \$440 million of forward equity contracts. This equity will be issued in connection with the acquisition of the facility and we have assumed the associated EPS dilution in our full year guidance.

While we don't have any further required financing needs at the parent this year, we will continue to evaluate opportunistic financings to derisk our future funding needs if market conditions are accommodative. Our approach to our financing plan is similar to how we run the rest of the business. We plan conservatively and capitalize on opportunities as they arise. This approach has been tried and true year in and year out and has enabled us to deliver on our operational and financial objectives, irrespective of the circumstances, to the benefit of our customers and investors and this year is no different.

And with that, I'll hand it back to Garrick for his final remarks before the Q&A session.

Garrick J. Rochow
President, CEO & Director

Thank you, Rejji. As you look at Slide 9, I'll remind you again, our track record spans 2 decades of consistent industry-leading results despite changing commissioners, legislatures and governors, recessions, severe weather and storm activity, or a pandemic. We're here for the long haul. We have powered Michigan's progress for nearly a century and a half. And as we look ahead, we see great opportunities to support the state's growth through critical infrastructure as we help power Michigan through the next century.

With that, Bailey, please open the lines for Q&A.

Question and Answer

Operator

[Operator Instructions] Our first question today comes from the line of Jeremy Tonet from JPMorgan. Please go ahead, Jeremy. Your line is now open.

Jeremy Bryan Tonet

JPMorgan Chase & Co, Research Division

And just wanted to come back to the key focus, I think, in the market at this point, just with the adverse weather and storm headwinds in the first quarter. Great to see that you're still targeting high end of the guide there. And just wondering, as you think about contingency flex this year, I guess, if there is anything else that moves against you, do you have more contingency that could offset that if weather shapes up less than expected or anything else moves against plan?

Garrick J. Rochow

President, CEO & Director

I have confidence in our ability to deliver. That's the first point, Jeremy. And we know there's a lot of year remaining. And so really in all our efforts, we look to build contingency out -- throughout the year. And so maybe if I just take a step back because I know this is a popular question today and just talk about our playbook. Rejji alluded to it but let me offer a little more specifics. And I'd break it into really 5 areas.

The first one is, we plan conservatively. And you know this, Jeremy. We've done this year after year after year. That's what leads to our consistency, one of the reasons we had consistent financial performance. And also, we talked about this in Q4. What we did in 2022 to derisk the year. And then just adding Rejji's points, we budget for storms, and we budget conservatively for storms because we know they occur throughout the year. And so in many cases, this is just a weather story. So the first piece is just we plan conservatively.

The second piece of the plan is the CE Way. And you -- this is another strong suit for us. And I'll remind everybody, it's industrial engineering and it's a lean operating system. It's science, it's proven throughout the years, for many different companies. And I see a great opportunity that we continue to deliver on year after year. Scheduling optimization is one example underway right now. We're making capital IT investments to get other efficiency improvements. It improves customer satisfaction while reducing costs. Our run rate has typically been around \$50 million a year, as you know, there's a lot more muscle we have there.

The third piece is really around the labor piece. And that is what you expect. We released some consultants. Our contractors are flexible, so we dialed that down a bit. We pinch back on overtime and then we hold on hiring. And so those things help as well.

The fourth area is really discretionary spending. It's limiting conferences and travel and some of the training. And you think that's small but it's actually big when you apply it across the entire company.

And then the fifth piece and Rejji hit on it, was good tax planning and just opportunistic financing. And so that's the recipe. And as I said, this isn't our first rodeo. If you go back to the pandemic, we had to find \$100 million. 50% of it came through the CE Way, 50% through other actions, very similar to what we're doing right now. And so we're going to chin this bar and we're going to add some contingency throughout the year.

So I feel very confident in our ability to deliver and to weather whatever Mother Nature throws at us throughout the year.

Jeremy Bryan Tonet

JPMorgan Chase & Co, Research Division

Got it. That's very helpful. And maybe pivoting -- maybe pivoting to the gas case. Just wondering if you could talk a little bit more about that. I know the gas case maybe -- it doesn't come as much focus as electric, generally speaking. But what are the key focus points across stakeholders in the gas case at this point? And just trying to get a sense for your thoughts on chances for a settlement without getting too far ahead of yourself.

Garrick J. Rochow
President, CEO & Director

First things first, this is a good and constructive starting point. If I were just to dissect it a little bit for you, what we saw from staff and the AG as far as ROEs was better than previous staff and the AG positions. And so that bodes well for an ROE and some of the financial metrics. The other important piece is, we build that -- remember, we built that case over Q3 and Q4 last year. And so gas prices were rising. We also saw some expense from pension and OPEB perspective but when you fast forward to today, those have changed. And so gas prices are lower. We snapped the line at the end of the year on pension and OPEB expense.

And so we got a \$212 million ask and that effectively pulls that down because the fact pattern is different than what we saw when we built the case. And then the big piece is that people are talking about here is the sales forecast. And there's about \$10 million, \$12 million difference there. And so let me walk through that. We have used this method since 2010 to project sales. It's a 15-year regression type model. We haven't changed it a bit. It's tried and true and it's accurate. And here's the important point. Back in 2010, the commission ordered us, let me repeat, the commission ordered us to use this method.

That was in case U-15986. And so we're doing exactly what the commission told us to do. So we feel like really good about where we're positioned there. And so there's a lot of cats and dogs but bottom line, take this away, it's a good constructive starting point. The other thing you asked about settlement, we'll always look for the opportunity for settlement but again, we sit in a very constructive jurisdiction. So I'm very comfortable taking it to the end and getting a full order from the commission.

Operator

The next question today comes from the line of Shar Pourreza from Guggenheim Partners. [Operator Instructions]

We will move on to our next question. Our next question today comes from the line of Julien Dumoulin-Smith from Bank of America.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Hopefully, strike 2 works here. You -- can you hear me?

Garrick J. Rochow
President, CEO & Director

We can, Julien.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Excellent. Let me follow up on the first question here just around the uptick in usage, nonutility tax and other. You guys elaborated on it. So not only have you pressed some of those levers to see the quarter-over-quarter change in '23 and the range, right, you're talking about \$0.36 to \$0.42 of positive offsets there now. But in addition to that, you've got further levers to go to the extent in which that they might materialize. I just want to make sure I understand the comment from earlier.

Rejji P. Hayes
Executive VP & CFO

Julien, this is Rejji. Yes, you've got it exactly right. And Garrick, I think, offered a wonderful dissertation on how we approach cost reduction opportunities. The only thing I would add to his comments is that when it comes to cost reduction, we don't discriminate and we look across the entire cost structure. When you exclude depreciation, it's about \$7 billion annually and about \$1 billion of that is a combination of interest expense and tax related spend, combination of federal, state income tax, as well as property tax. And so we look across all of those cost categories to identify opportunities. And what you're seeing in that penultimate bar in that waterfall are opportunities that we anticipate around potential prefundings.

As you know, we aggressively look at the maturity profile of our bonds and see if there are opportunities to take out bonds prematurely. So we'll look at those. And then again, on the tax planning side, we're always looking for opportunities to reduce costs, whether that's for state tax, property tax or otherwise. And so that's what's incorporated into that last item. And again, that's all I would add to Garrick's good comments on how we approach cost reduction.

Julien Patrick Dumoulin-Smith

BofA Securities, Research Division

Excellent and fair enough. And then just following up on some of the conversation on regulatory mechanisms. You talked about including an investment regulatory mechanism in your upcoming case. Can you talk about what that looks like? And perhaps talk about that in parallel with some of this conversation on ring fencing here? I mean how do you think about ring fencing to isolate spending on specific subject areas, where it sounds like this, the IRM might be related? And then Also, maybe you could talk about ring fencing in the context of veg management efforts.

Garrick J. Rochow

President, CEO & Director

Absolutely, Julien. And you've obviously listened to the Chair Scripps, he's used the word ring fencing around some of the capital investments. So the way we think about it is really, I'd put it in 3 buckets. And so the first bucket is really, we know that in order to deliver reliability and resiliency for our customers, that's going to take more capital investment. It's just the nature of an aging systems with more severe weather. And so we're all focused on that. The commission -- we're certainly focused on the company. And so is every one of our coworkers here within CMS Energy and the broader Consumers Energy. So we're squarely focused on that first bucket.

The second bucket really is, is what you brought up and that's the commission wants to be able to ring fence it. And they're looking at the prudence, accountability. And typically, when we've asked for large increases, they want to know that we can do the work, that we have the resources to ramp up. And so that's an important piece. And this IRM, well, this tracking mechanism allows us to do that and provide the accountability that the commission is looking to see.

And so ultimately, that should lead to the third bucket, which is the recovery piece, which is helpful for investors. And so I see all those 3 working together. And in fact, I want to give you an example. Back in 2011 and I was engaged with it in 2011, we did a similar on our gas business. We were looking to increase the amount we spent on replacing mains and services. We started a new gas construction group. And the commission and staff at the time were -- had questions about -- important questions about how you're going to do that and how are you going to ramp up the resources. And so we did a similar type mechanism then, delivering improved safety for our customers, replacing mains and services and creating that ring fence, that accountability associated with the tracking mechanism.

And we were very successful. It started out at \$85 million back in 2011 and now it's a \$250 million program on an annual basis. And so we're taking that same approach as we go through this case. Is that helpful, Julien?

Julien Patrick Dumoulin-Smith

BofA Securities, Research Division

Yes, absolutely. So perhaps let me just make sure I'm hearing you right. This IRM, would that help address some lag related considerations, perhaps shift timing of future cases? Or is this principally about

accounting and accountability back to the commission to just make sure the dollars and cents are getting spent in the right bucket?

Garrick J. Rochow
President, CEO & Director

The latter is the main focus. And then -- I mean over time, it could lead to extend out some rate cases. But our focus right now is just making sure there's the accountability piece and the ring fencing that our -- that the Chair has referenced in some of his public comments.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Got it. Excellent. And then on veg management, just quickly, just with respect to that side of the equation, obviously, been a lot of focus on that front. Your commentary saying that you've increased it from 2020, helpful. Any further efforts in that regard? Again obviously, there seems to be an acute desire or need for that. How do you think about allocating even more in that direction at this time?

Garrick J. Rochow
President, CEO & Director

Yes. So just to give you some real numbers on this, so about -- in 2020, it was around \$50 million on an annual basis. And with support of the commission through different cases, we requested more to address this important aspect of reliability. We were up around \$100 million on an annual basis. And there's a couple of components of it. And we're continuing to look at other opportunities to invest more in that. But we're also looking at the efficiency of that and so this is an area where we're using technology and artificial intelligence and analytics to be able to better predict where to utilize those dollars.

And so we've -- our trees trimmed per mile has actually improved over the time period as well. And so that's helpful in the conversations we have with the commission. And then we'll continue to look for opportunities to look at other areas to invest and improve reliability, much like I said during my comments around the capital investments. I know Rejji wants to add to it as well.

Rejji P. Hayes
Executive VP & CFO

Yes, Julien, the only thing I would add is that when we think about the planning year and particularly years in which we have a little bit of upside or contingency, usually vegetation management is one of the first items that comes up on the flex list. And last year, in fact, when we were -- had a little bit of upside that was weather driven, we did about \$5 million or so of flex related to vegetation management. So our actuals, even though we've budgeted around \$100 million, as Garrick noted, for last year, I think our actuals were closer to \$105 million, certainly over \$100 million. And so flex is an opportunity for us to do additional vegetation management. And then remember, we have that voluntary refund mechanism, which is also a vehicle through which we can do incremental operating expenses.

And so the current voluntary refund mechanism that we have outstanding, we targeted about \$8 million towards additional vegetation management this year out of the \$17 million that we allocated to the electric business. And as you know, we obviously pulled that lever in Q4 of last year for \$22 million all in. And again, a portion of that will be allocated towards vegetation management, assuming we get commission approval. So that's the other mechanism we have as well.

Operator

Next question today is a follow-up question from Shar Pourreza from Guggenheim Partners.

Shahriar Pourreza
Guggenheim Securities, LLC, Research Division

Sorry, if I missed this but I just wanted to maybe just round out the storm discussion. I guess, do the storms -- do they -- will they lead to more resiliency spend? Is it going to increase CapEx? Or do you see

offsets to CapEx? Are you going to sort of seek any kind of new mechanisms? I mean, some things are already in rider-like items. Would resiliency kind of get that similar treatment? I guess overall, just how do these storms kind of change your thoughts around the 5-year plan?

Garrick J. Rochow

President, CEO & Director

We, Shar -- so just to be really crystal clear on this, there's going to be more capital investment that's needed to improve reliability and resiliency and it's a reflection of an aging system with more severe weather. And I offered some of that in my prepared remarks but in this next electric rate case, we're proposing IRM or investment recovery mechanism as a tracker to show in greater certainty around our capital investments. And so that's the intent. We know we have to invest more. There's a number of ways to do that. One is our storm audit and focusing on that and getting alignment with the commission. And the other is the rate case and then the other one is the 5-year electric distribution investment plan.

And so all of those different filings, all those different conversations lead to better alignment and a better support for our electric distribution investments. And so the long term is yes, in that. And this IRM mechanism, we believe, will create greater accountability with the commission. Chair Scripps has talked about ring fencing and then ultimately should lead to more recovery of those capital investments. Is that helpful, Shar?

Shahriar Pourreza

Guggenheim Securities, LLC, Research Division

Yes. And I guess the question is, should we be looking at these incremental investments as extending the runway of your growth or accretive to your growth?

Garrick J. Rochow

President, CEO & Director

We have a long runway and we invest -- we update our plan every year. But that 5-year plan includes about \$6 billion of investments in the electric distribution system. That is up. That was up in this most recent plan. And we'll continue to look at as we model across the system, as there's additional investments, we'll continue to look at opportunities to invest more there. There's a long runway of opportunity just given the nature of our system.

Shahriar Pourreza

Guggenheim Securities, LLC, Research Division

Got it. And then maybe just shifting to financing. Financing is -- it's been a bit of a tough headwind but interest rates seem to have moderated year-to-date. I guess how are you trending versus the embedded interest cost and plan in terms of '23 and maybe even opportunities for some cushion versus '24 since rates have come down versus your original expectations?

Rejji P. Hayes

Executive VP & CFO

Yes, sure. This is Rejji. Great question. So as always and I think we had a word count of about 6 or 7 times in our prepared remarks, where we talked about planning conservatively. And that has been the case here. And so in our plan, we had pretty conservative assumptions at the operating company and that's where the vast majority of the issuances are this year. And we've been fortunate for the issuances we've done to date, to issue those at levels -- interest rate levels below what we haven't planned. So we're seeing upside and that's already flowing through our '23 numbers. And obviously, we'll benefit from that in '24 and beyond because we're issuing long-dated paper.

And so certainly, with interest rates moderating over the last several months, that creates additional opportunities. And that's what we'll be mindful of as we look at the final sort of 6, 7 months of the year and seeing if we can capitalize on, I'll say, the accommodative capital markets that we're seeing right now.

Operator

Next question today comes from the line of Durgesh Chopra from Evercore.

Durgesh Chopra

Evercore ISI Institutional Equities, Research Division

Just maybe on the -- just continuing the discussion along storms, can you update us on the investigation that was started by the commission? My understanding is that they were looking for third-party consultant. So maybe just what's the latest there?

Garrick J. Rochow

President, CEO & Director

Yes, broadly, from the storm audit perspective, so they started that last fall. And so they're in the process of selecting the vendor right now or the firm right now. We anticipate that to start in the September time frame. But I'll remind you the big picture perspective on the storm audit, is that, we're both aligned. That being the commission and CMS Energy aligned that we need to improve reliability. And so I really view this as an opportunity to be able to get further alignment on the needed investments in our system.

I'll give you a great example in undergrounding. We want to do more undergrounding. And if we look at our Midwest peers, they're around 35%, 40% underground. We're at 10%. It goes back to Shar's question. Is there opportunities for investment? There's a lot of them. And so we see that as important -- you can look at the EPRI, Electric Power Research Institute and they'll say undergrounding improves reliability, depending on if it's 3 phase or single phase by 50% to 90%. And so this is a great example where we need -- with the storm model, we can utilize this to get better alignment on the needed investments in the system.

And once we have that alignment, then again, we can move forward and get greater certainty around those investments. Does that help, Durgesh?

Durgesh Chopra

Evercore ISI Institutional Equities, Research Division

Absolutely it does. But you don't -- I guess the point is, I know you've said this before, you don't see anything punitive coming out of those audits as a result as they kind of go through your processes and other things and best practices?

Garrick J. Rochow

President, CEO & Director

I don't see anything punitive. No.

Durgesh Chopra

Evercore ISI Institutional Equities, Research Division

Got it. Okay. And then just one quick follow-up. I know this is small but you've got a decision on the voluntary refund mechanism earlier in the month. And I believe there were some disallowances. Can you talk to that and discuss that briefly?

Garrick J. Rochow

President, CEO & Director

Yes. I'll tag team it with Rejji. Just a context around this. These are pretty small dollars. And the bottom line, we have this option to file a voluntary refund mechanism. And we did that in 2022, the dollars are booked in 2022. But it's not a cake walk, like it's not assured that you're going to get approval, staff and the commissioners have a say in that, right? And they really telegraph the importance of incremental forestry and some other things with our customers in terms of helping out those low-income customers.

And so they've really given us another opportunity at the bat. And we filed that here on April 21 to reflect the commissioners' and staff's comments. And so I feel good about getting to a positive outcome on that and it's just navigating kind of the back and forth of the process, Durgesh.

Rejji P. Hayes*Executive VP & CFO*

Yes. That's the essence of it, Durgesh. Just to give you some specifics on the numbers. So when we filed the VRM in late 2022, it was for \$22 million, \$5 million of which was to support our vulnerable customers on the gas side of the business. That was fully approved by the commission and where there was some, I'd say, counsel and guidance by the commission was on the balance of the \$17 million that we allocated to the electric business. And to Garrick's comments, they wanted to see direct customer benefits. And so that's why we have recently, as of last Friday, requested service -- sorry, additional forestry or vegetation management as well as additional support for vulnerable customers.

So that's how it's cut. Just that \$17 million is subject to further approval and we're confident that we'll get this recent request over the finish line.

Operator

Next question today comes from the line of David Arcaro from Morgan Stanley.

David Keith Arcaro*Morgan Stanley, Research Division*

Let's see, there's been some legislative bills drafted in the state with some more aggressive net zero targets. I was wondering if that might impact any of your thinking around the next time you address the IRP?

Garrick J. Rochow*President, CEO & Director*

Great question. Let me -- I think perspective is really important here because often in Lansing, just part of a bill, there's a lot of back and forth and there's media releases and then you just got to kind of clear the air and talk about it from a big picture perspective. And so I'll remind our listeners here that in the governor's first term, she introduced the Healthy Climate Plan. And in fact, one of the members on my direct staff was one of the stakeholders in that process and was involved in the review and kind of the language around it. And then I participated with a group of about 8 to 10 CEOs and the Governor in the review process.

And so that -- her -- the Governor's healthy climate plan lines up really well with where we're headed from a state perspective but also lines up well with our current IRP and the like. Now the legislature has -- the Senate specifically, has introduced some new bills that are little bit more aggressive. But I want to remind everybody, this is the back and forth of Lansing.

And that's the first starting point. That's the first volley you might say. And so we're going to continue to navigate that and move forward with that and manage that process. Ultimately, at the end of the day, if it requires something -- for us to do something sooner, we'll do that sooner. And that will mean more capital investment opportunities. But I want to let everyone know it's really manageable and, again, well aligned with where we're already headed.

David Keith Arcaro*Morgan Stanley, Research Division*

Got you. That's helpful. And could you also touch on just what you're seeing in terms of weather normal volumes -- the sales volumes and how that's lining up with your expectations so far?

Rejji P. Hayes*Executive VP & CFO*

David, this is Rejji. Appreciate the question. Yes, weather normalized trends, I will admit, we were scratching our heads a little bit at the trends that we saw. And just for everyone's benefit, we saw residential about 2.5 -- a little over 2.5% off versus Q1 of 2022. Commercial, a little over 3.5% off versus

Q1 of 2022. Industrial was flat excluding 1 large, low-margin customer. And then total was down about a little over 2.5% versus Q1 of last year. And I would say it's really early days.

We are still digging into the data. I would just start by saying, as hard as our sales forecasting team works, weather normalized math is a combination of art and science. And when you see, I'd say, dramatic weather like we saw in Q1 of last year, where it was extremely cold and then a pretty warm winter as we noted earlier, Q1 of this year, you can see a good degree of imprecision in those calculations.

And so I say -- all that to say, we're looking at it with a little bit of a skeptical eye because the reality is we're still seeing very strong economic indicators in the service territory. Our customer accounts specifically for commercial, were up almost 0.5% -- over 0.5% to almost 1 point across the electric and gas businesses, residential customer accounts are still up. And while we have built into our guidance, that continued return to work, we're still seeing a good level of really not every company in Michigan at this point has 4, 5 days in the office. And so we still think as we get into the summer months, we may see some of that favorable mix we've seen in the past.

And so I would say early days, there's probably a little bit of noise in the data. And I'll just say on the industrial side, we were flat again versus where we were last year but we couldn't have a more robust economic development pipeline borne out of a lot of the constructive federal legislation that's been passed over the 18 months. And we continue to look at our trends versus pre-pandemic and across every customer class we're doing as well, if not better, than what we were doing pre-pandemic, particularly when you take into account our energy efficiency programs, which effectively reduced our load year-over-year by 2%.

And so, again, I don't think what you're seeing in Q1 and in the data is indicative of the economic conditions in Michigan. I think it's just more weather-normalized math versus anything else.

Operator

Next question today comes from the line of Michael Sullivan from Wolfe Research.

Michael P. Sullivan
Wolfe Research, LLC

You guys answered a lot here. I just had a couple of small follow-ups on what's already been discussed. So just on the undergrounding, can you maybe just give us a sense on what the long-term target is there? How much of the system you are looking underground and over what period of time you'd like to get there?

Garrick J. Rochow
President, CEO & Director

Great question. And it's important to recognize we're not trying to underground the entire system and it's really about selective or sometimes I've used the word strategic undergrounding. And again, we know from EPRI research across a number of utilities, you're in a 50% to 90% improvement, whether it's 3 phase or single phase. And so ideally, we're trying to get to a point where we can do 400 miles a year. And then really over a 10-year period, kind of increment that up.

So I would say the range of around 10,000 miles is really what we're trying to get to overall. It's not going to occur overnight but that does provide a nice opportunity to enhance the reliability and resilience of our system and provide a nice opportunity from a capital investment standpoint.

Michael P. Sullivan
Wolfe Research, LLC

Okay. Very helpful. And then kind of a similar question just following up on the IRM. I think the context you gave on the gas side was helpful in terms of where it started and where it's gotten to. Can you maybe frame that on the electric side? And I know you haven't officially filed the next case yet but just kind of where that could start and ultimately go?

Garrick J. Rochow

President, CEO & Director

So we're being very thoughtful about our starting point and we see it as an opportunity to grow from there. But our first volley will be in the \$100 million range for an IRM and then we'll grow it from there.

Operator

The next question today comes from the line of Andrew Weisel from Scotiabank.

Andrew Marc Weisel

Scotiabank Global Banking and Markets, Research Division

Let me first say congratulations again for selling EnerBank. I'm very glad we're not spending 3/4 of the call talking about that.

Garrick J. Rochow

President, CEO & Director

I'm glad too. Thank you.

Andrew Marc Weisel

Scotiabank Global Banking and Markets, Research Division

Yes. First question, just a follow-up on undergrounding. So you talked about the 50% to 90% operational improvement estimate from EPRI. Do you have a rough sense of rule of thumb, the cost difference versus traditional [underground spending], what a breakeven might look like?

Garrick J. Rochow

President, CEO & Director

So what are the things -- we're doing some -- we've done a lot of -- we shouldn't say a lot but we're doing a lot of work with our undergrounding crews right now. And that price for undergrounding, particularly on a single phase, is approaching the price of overhead. It's not quite there yet but close. And so we're in the range on single phase maybe like \$250,000 a mile for undergrounding. Again, it's directional bore. And give or take, it depends on the conditions of the soil and homes and other things but that's roughly the number.

And so they're really quite comparable or growing comparable in terms of that price point. And so again, we've got pretty fertile soils. We have pretty soft soils. And so we're not in rock and some of those things, which helps from a cost perspective.

Rejji P. Hayes

Executive VP & CFO

Yes, Andrew, the only thing I would add to Garrick's comments, when you think -- the only thing I would add to Garrick's comments, when you think about the cost benefit and the potential opportunity, if you look at the last few years of our vegetation management plus our service restoration, we're spending on average based on actuals about \$200-plus million per year across those two cost categories. And so the opportunity would be over time with those investments in underground and to potentially reduce that overall cost bucket.

And so that's how we would think about the cost benefit in addition to some of the points Garrick raised earlier.

Andrew Marc Weisel

Scotiabank Global Banking and Markets, Research Division

Okay. Great. Next one, are you able to tell what's the deferred fuel cost balances now versus at year-end?

Rejji P. Hayes

Executive VP & CFO

Yes, I'll take a stab at that, Andrew and we can follow up with more precision on -- offline, if needed. Where we ended the year, we had -- well, goodness, end of 2022, just over \$800 million across our power supply costs in the electric side and then gas inventories on the gas side of the business. So call it about a \$450 million, \$400-ish million split, so it's \$850 million. We started to chip away at that. Obviously, we have very strong cost recovery mechanisms in Michigan, which have been kind of tried and true since the mid-'80s. And so we do expect on the gas side to recover the vast majority of that over the course of this fiscal year.

And then for electric, we did apply a bit of elegance to a recovery process for power supply cost. And so of the \$450 million we had coming due in January, we filed with the commission a plan to recover that over a 3-year span. So effectively \$150 million per year through 2025. And just given the current environment, we thought that, that was the right thing to do to alleviate the cost burden for customers. And we also thought our balance sheet could accommodate it as well.

And it's also the way we structured it, just that the fact that we're no longer going to be recovering those costs through working capital, now through regulatory asset, it's actually credit accretive based on how Moody's calculates these -- their FFO. And so for a variety of reasons, it was a nice opportunity and we've exercised it in the first quarter.

Andrew Marc Weisel

Scotiabank Global Banking and Markets, Research Division

Okay. Good. One quick follow-up, if I may. Palisades, I know there's not a whole lot new for you to announce but can you just give an updated thought on the timing of potential updates there with the state versus the timing of your next IRP, which I believe is likely to come next year.

Garrick J. Rochow

President, CEO & Director

So we do know -- I mean, it's public information that Holtec, who is responsible for decommissioning the facility and has the operating rights there on the facility, has requested federal funding. They've also requested state funding within this budget, which is being worked right now, state budget. So that will be figured out this May, June, July time frame. They've asked \$300 million in the state budget. Again, this is public information.

What I would expect to see from this is a lower cost for power. We've had Palisades, it's been an expensive PPA, one would expect it to be lower given all the tax dollars that are applied there. And that power should flow into Michigan. So those are important components of it. So we expect low-cost power, as I've said historically and we're open to consider a PPA with the financial compensation mechanism. But at this point, we got a good IRP in place. And if that comes to fruition, it will shape our next IRP. But it's really too soon to tell on how it would shape upcoming IRPs.

Andrew Marc Weisel

Scotiabank Global Banking and Markets, Research Division

Okay. I guess the more specific question was, would the timing of your IRP potentially be influenced by the timing of Palisades resolution?

Garrick J. Rochow

President, CEO & Director

That's too hard to tell. And frankly, this -- bringing a nuclear plant back has -- to my knowledge, has not been done. And so there's a lot of hurdles and a lot of unknowns there. I'm not saying it can't happen but there's just a lot of unknowns. And so it's difficult to say whether it will have an impact or not on our next IRP.

Operator

Next question today comes from the line of Alex Mortimer from Mizuho.

Alexander Mortimer*Mizuho Securities USA LLC, Research Division*

And so given that everyone in the industry is kind of always walking the tightrope between reliability and then customer bill impact, can you provide sort of any thoughts on what the tone of the commission has been with regards to the undergrounding? Is this something that, that they've suggested or something you're sort of bringing to them unprompted?

Garrick J. Rochow*President, CEO & Director*

There's been a lot of conversations and there will continue to be more conversations on this important work of undergrounding. We'll be doing some additional piloting within the context of this proposed electric rate case. And then we'll continue to look at other opportunities to build out on that. But going back to the storm audit, this is really our opportunity to get further alignment with the commission on the important investments that need to be made to improve reliability and resiliency. And I would suggest that both the commission, staff and the company and all our coworkers here, too, are really well aligned on ensuring that we're improving reliability and resiliency.

You talked about the affordability piece as well. And that's clearly at the top of mind. Part of that is, we leverage the CE Way, not only to improve our operations and maintenance expense but we utilize it to improve capital efficiency. So that dollar goes further. Just like I shared earlier, we continue to look at opportunities to bring the cost down of undergrounding and frankly, all our capital work.

Alexander Mortimer*Mizuho Securities USA LLC, Research Division*

Understood. And just a little bit more color on sort of the time line of what this would look at or what this would look like and then potentially the dollar amount of upside to the CapEx plan? And should we think of this as getting you kind of into the high 7s, towards 8% of your long-term guidance? Or is this more of extending the 7% out beyond sort of where it is currently?

Garrick J. Rochow*President, CEO & Director*

So when we introduced in Q4 call, we introduced our \$15.5 billion capital investment plan. And that had more electric distribution, electric related spend in that plan was like \$6.1 billion of that, which was an increase. We're not changing our capital plan at this point because we increased it just here in the last call. That may change over time because we look at that capital plan every year. And as I've shared, there's a long runway of opportunity there. And so as we get certainty around these investments, as we build out that 5-year electric distribution plan, that will be an opportunity to look at the longer-term capital piece.

Now going back to the growth piece. 6% to 8%, we said confidence towards the high end and that puts it in that range of 7% to 8%. Historically, I've said this, I'll say it again, there are no sugar highs and we go for consistency year after year. And so that's -- we compound off actuals. That's the quality of earnings that we aim for and we will continue to repeat year after year, because we know that's what our investors value.

Alexander Mortimer*Mizuho Securities USA LLC, Research Division*

And congrats again on a great quarter.

Operator

The next question today comes from the line of Ross Fowler from UBS.

Ross A. Fowler*UBS Investment Bank, Research Division*

So just a couple for me here. One, the first part is, just any commentary on Commissioner Phillips resignation and time line for replacement, thoughts on replacement. And then Garrick, not to beat the dead horse here but you came into the year -- on my quick math, it's about \$75 million of cost contingency to offset the sort of weather normalization you knew you were going to have to deal with. Now Garrick, as you went through those 5 things, you've priced that up to about \$200 million on a round number. So there's another \$125 million or so coming in. And clearly, you thought about what's in that bucket that's onetime and what's sort of more permanent.

Maybe can you contextualize for us how conversations with the commission has gone around what's onetime cost improvement, what's permanent improvement in the past, so you kind of look to the future as to how those negotiations go because clearly, there can be some conversation around that as you look at the cost reduction?

Garrick J. Rochow
President, CEO & Director

Let me start with Tremaine Phillips. And it was -- I have great respect for Tremaine. He was a great commissioner and we saw constructive outcomes. And he left a legacy at the commission and I'd put it into 3 areas. One, he really moved electric vehicles in the state. And he was forward-thinking and progressive about that work. And then in addition to that, there was a lot of work on grid monetization and optimization of the grid that he helped position within the commission. And the third piece, and this is -- it really played out nicely over the course of the pandemic is, he was laser-focused on low income and vulnerable customers.

And I give him credit, as well as the commission for the work -- we have the lowest bad debt levels across the industry. And so we've taken care of our low-income customers during some of the toughest times during this pandemic. And so much of that credit goes to Tremaine Phillips. But I'll also refer you to -- he's got a public statement out there. He's successful but so is his wife, is successful. And his wife has went after new opportunities and so many thanks and congratulations to both Tremaine, his wife and his family as they pursue different career opportunities.

This commission has functioned well in the past with 2 commissioners. And we've got 2 constructive, experienced commissioners in place. And so I'm not worried about the interim at all. And if you look historically as well as with this governor, Governor Whitmer here, they've been very thoughtful about the placement of commissioners and found experienced and well-suited commissioners to continue the constructive environment, regulatory environment in Michigan. We do know that the Governor is out -- the Governor's staff is out looking for a new commissioner. That process is underway but we don't have a deadline or a date out there on when that will take place. But again, I have confidence in our Governor to continue the long-standing tradition of this jurisdiction and a constructive jurisdiction.

I'm going to pass the call over to Rejji here to talk a little bit about the financial information to your second part of your question.

Rejji P. Hayes
Executive VP & CFO

Ross, I appreciate the question. So just one last thing on Tremaine and it's a bit of an advertisement for the Michigan legislative and regulatory construct. I mean, part of the reason why it's really wonderful to have staggered terms for your commissioners is because when you do have turnover on an unexpected basis, you still have that continuity of leadership. And so we obviously have Chair Scripps and Commissioner Peretick still in the seat. And they obviously have a policy -- or their philosophies are aligned with the governor's policies, I should say, around healthy climate. And so there's that nice continuity there and they have a quorum with 2. And so we'll still carry on and I'm sure they'll find a suitable replacement for Commissioner Phillips when the time is right.

With respect to your question around the cost opportunities, let me just be very clear, I'll try to get at the numbers you specified as best I can. And if I miss anything, please feel free to follow up with a question. But if you think about our guidance at the beginning of the year on our Q4 call, we effectively said, as

always, we plan for normal weather. And we assume the level of cost productivity in our plan. And so we were showing about \$0.04 per share of positive variance related to cost savings. And then we had some estimated opportunities as a result of the warm weather we put to work in 2022 in Q4 specifically with the voluntary refund mechanism and some of the pull aheads and opportunities we exercised in the context of the electric rate case settlement.

And so that equated to about \$0.19 to \$0.25 of opportunity or positive variance in the original guidance. And so as you fast forward to Q1 and you look at the waterfall we're showing today, what's really changed is that we've now seen \$0.21 or just over \$80 million pretax in the form of weather hurt and that's what we're offsetting or solving for in the form of cost productivity as well as in that sort of catch-all bucket around parent-related opportunities. And so what we're effectively saying is that there is \$80 million of offsets that we need to go identify and when we look at our track record and we're not trying to be immodest around that, we feel very good about our ability to achieve that. And so when you think about 2020, during the pandemic, we took out \$100 million.

And when you think about sustainable savings versus one-timers, about 50% of that in 2020 was in the form of the CE Way, and that's what will flow through rates. And that's what customers will benefit from. There are one-timers that sometimes we do have to resurrect some of those old plays. And so those are sort of opportunities that probably don't get incorporated into rates because you need to execute on those in subsequent years. But my working assumption is we'll see probably about a good portion of the opportunities we're trying to execute on and offset this \$0.20 or \$0.20-plus of weather in the form of CE Way as well as those opportunities Garrick noted earlier in the call.

So whether it's hiring freezes, whether it's external hiring type decisions around contractors and consultants, we will take all of those opportunities as part of this portfolio of savings to offset that, call it, \$80-plus million of weather. So that's how we think about it. That's how we'll go get it. And again, a good portion should be passed on to customers but some will be one-timers and those are the ones that you don't necessarily repeat. Is that helpful?

Ross A. Fowler

UBS Investment Bank, Research Division

Yes, that's helpful, Rejji. I guess in the past, you've been able to have that discussion with the commission. It's really onetime and was permanent, in the context of any debate around that, right? As you look at some of that CE Way money and then some of the sort of hiring freeze stuff, I guess the risk from my perspective is the commission would say, well, you have a bunch of onetime stuff in there and some of that permanent, can we get some customer bill relief out of that more permanent basis. But maybe contextualize that risk around discussions you've had about that in the past and their understanding of what's onetime and what's not.

Rejji P. Hayes

Executive VP & CFO

Yes. To be clear, this is the benefit of filing annual cases because as we realize those savings, which again, when they're generated the CE Way, they are sustainable, we will pass them on in subsequent cases or as part of the adjudicated process. Because when we file rebuttal, we start to bake in some of those savings midstream. And so there is a pretty transparent dialogue with the commission staff and other interveners about the opportunities we think are sustainable, and that's what we incorporate into our cases. And again, that's the benefit of being an annual filer.

Ross A. Fowler

UBS Investment Bank, Research Division

Fantastic. So I'm with you on the \$80 million in cost cuts and then there's like an incremental \$50 million between the sort of year-end call back in this deck and that other usage category kind of went through in the answer to Julien's question.

Rejji P. Hayes

Executive VP & CFO

Yes. The only other thing I'll mention, just to be clear, there is a bit of geography, you have to be mindful of as well. So when we say parent-related savings, whether they're tax planning or financing efficiency, some of that is at the holding company, in which case, it wouldn't be incorporated into an adjudicated process because they're not at the opco level. So some of those will directly go to shareholders. And so I think that's also very clear to the commission and other stakeholders in the context of a rate case.

Operator

No additional questions waiting at this time. So I'd like to pass the call back over to Mr. Garrick Rochow for any closing remarks.

Garrick J. Rochow

President, CEO & Director

Thanks, Bailey. I'd like to thank you for joining us today. We'll see you on the road soon. Take care and stay safe.

Operator

This concludes today's conference. We thank everyone for your participation.

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