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DTE - Q4 2017 DTE Energy Co Earnings Call

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OVERVIEW:

Co. reported 2017 earnings of $1b or $5.59 per share. Expects 2018 EPS to be $5.57-5.99.

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PRESENTATION

Operator

Good day, and welcome to the DTE Energy Year-end 2017 Earnings Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Barbara Tuckfield. Please go ahead, ma'am.

Barbara Tuckfield *- DTE Energy Company - Director of IR*

Thank you, Alecia, and good morning, everyone. Before we get started, I would like to remind everyone to read the safe harbor statement on Page 2 of the presentation.

Our presentation also includes references to operating earnings, which is a non-GAAP financial measure. Please refer to the reconciliation of GAAP earnings to operating earnings provided in the appendix of today's presentation.

With us are Gerry Anderson, Chairman and CEO; Jerry Norcia, President and COO; and Peter Oleksiak, Senior Vice President and CFO. We also have members of the management team to call on during the Q&A.

Now I'll turn the call over to Gerry.

Gerard M. Anderson *- DTE Energy Company - Chairman & CEO*

All right. Well, thank you, Barb, and good morning, everyone. Thanks for joining us. So this morning, I'm going to give you a quick recap of our performance in 2017 as well as an updated preview of our performance in 2018, updated versus EEI last year. I'll also describe how tax reform impacts DTE and our customers, and then I'll turn it over to Peter, who will review our financial highlights and provide a bit more detail on the impact of tax reform on our 2018 guidance. And then finally, Jerry Norcia will provide an update on our long-term growth plan, and he'll wrap things up before Q&A.

So we have a lot to be proud of as we look back on 2017, not only financially, but on many other fronts as well. And as I think will become clear to you, my confidence is high that we are very well positioned for success in 2018.

So I'll start with a quick recap of our accomplishments in 2017, beginning on Slide 5. I think that those of you who have talked with me over the years know that I strongly believe that a company's success is ultimately determined by the strength of its culture. Well, the culture at DTE is very healthy, and that bodes well for the future. In 2017, our employee engagement was in the top 4% of Gallup's worldwide database, and that's the highest employee engagement score we have ever achieved in our 20 years of tracking engagement here at the company through Gallup. Early in 2017, we earned our fifth consecutive Gallup Great Workplace Award. We remain the only utility ever to receive it, and we hope we're positioned to receive our sixth consecutive award early this year.

We also had one of the safest years in the company's history. We received the American Gas Association's Safety Achievement Award for the second year in a row. Safety is a priority for obvious reasons, but it's also a great indicator of your employees' level of focus and their discipline.

We produced some very strong results for our customers in 2017 as well. Both our electric and gas companies were ranked highest in customer satisfaction with business customers in the Midwest in J.D. Power's 2017 study. And this is the first time in our history that we've held down 2 J.D. Power #1 trophies simultaneously. Additionally, we ranked second in overall satisfaction with electric and gas residential customers in the Midwest, and our combined ranking of #1, #1, #2, #2 is the best overall customer satisfaction outcome in DTE's history.

We continue to target improvements in these results, in the customer satisfaction results. And as we've said before, our biggest lever for achieving those improvements remains modernizing our grid and improving electric reliability. And with that in mind, we have made significant investments in recent years, including last year, to improve reliability. And I really feel those investments are paying off. And during 2017, our grid reliability was tested by the most damaging windstorm in our history with near-hurricane force winds gusting to 70 miles an hour, leaving nearly 40% of our electric customers without power. And during a massive restoration effort, we restored about 70% of our customers in 2 days and over 95% in 4 days, and that storm restoration effort earned us EEI's Emergency Recovery Award. And as I look back on last year, this storm restoration effort is one of the things of which I'm proudest.

Now I think you know that historic storms can bring companies in our industry to their knees and put them in the penalty box with regulators and customers, and we had the opposite experience last year. We achieved the highest customer satisfaction ratings in our history in the wake of this event, and that is the product of tireless effort of our employees to restore our communities as quickly as possible.

Storm was also a testament to our continuous improvement practices. We put a lot of effort into revamping our storm restoration processes, and it made a difference. And we're focusing those same CI disciplines on productivity and cost containment and efficiency. And the results of those efforts is our ability to have O&M growth that is among the lowest in the industry, which is helping to keep customer bills at levels that work.

I'm also proud, moving on to Slide 6, of our efforts to be a force for growth in the communities we serve. So these efforts earned us the #1 ranking in the Midwest for corporate citizenship by J.D. Power, and we are making significant investments in Michigan. We spent $1.7 billion with Michigan-based companies in 2017, which exceeded our commitment to the Pure Michigan Business Connect local supplier initiative. As I look back to 2010, when we started all of this, we were spending less than $0.5 billion a year with Michigan suppliers. So it's been a great effort, and our 7-year effort to increase spending with those suppliers has created nearly 16,000 jobs in our state.

We also announced a broad sustainability initiative in 2017 that will reduce the company's carbon emissions by more than 80% by 2015, setting in the process the long-term strategic direction for our power generation fleet and providing leadership on what I consider to be a vital public policy issue.

But we've always said that if you serve your customers well and if you manage your costs and rates well and if you're a positive force in your community, your odds of having constructive regulation are a lot higher. And Michigan's regulatory environment continues to be constructive. That said, I will say our commission has a lot on its plate right now. In 2017, Michigan began implementing the energy legislation that passed in 2016, which has significantly added to the workload of our commission. It's essentially added a second job on top of the many cases and issues that they normally work through. And our job is to keep working constructively with them to define good policy outcomes for Michigan.

And in that vein, in 2018, we have a few key priorities on the regulatory front. The first is working through how our customers will get a break on their bills from tax reform, which will provide a significant boost to our efforts to maintain customer affordability as we continue to invest heavily in modernizing aging infrastructure. Those tax reductions to bills are priority 1. The second is that we need to finalize the Certificate of Necessity for our 1,100-megawatt new combined cycle plant. So this plant, along with our renewable power investments, is the way that we will backfill the retirement of 3 end-of-life coal plants totaling over 2,000 megawatts that will come off-line in the early 2020s. And this gas plant is also an essential step in the carbon reduction plan that I just mentioned a minute ago.

And then finally, we need to achieve reasonable rate case outcomes, outcomes that allow us to continue to upgrade and modernize our infrastructure and invest in the cleaner generation I've just described and improve reliability for our customers. So I know you all follow our rate case proceedings closely. And as is often the case, there are other filed positions out there, but we do remain confident that we're in a position to get good, constructive outcomes in these cases that are consistent with our plan.

Now moving on to growth and value creation. As I've already mentioned, we continued to invest in renewing our utility infrastructure in 2017, and that will continue this year. Our nonutility businesses had a number of big wins in 2017. So at our Gas Storage and Pipelines business, our Bluestone pipeline achieved a 1 Bcf per day delivery milestone with additional expansions on the horizon. We made significant progress on the NEXUS Pipeline and its construction, and we remain on track for in-service late in the third quarter this year.

We also initiated 3 new projects at our Power and Industrial business, including a sizable energy service project with Ford Motor Company, where we will build on and operate a host of advanced energy systems to power Ford's research and engineering center, helping them to achieve a nearly 50% energy use reduction. Power and Industrial also closed 2 RNG, or renewable natural gas, acquisitions in 2017, which will produce renewable gas to be used in vehicle fleets to meet carbon reduction goals. In 2018 at P&I, we have a number of promising initiatives underway, and the same is true for GSP, and Jerry will touch on those a bit more later.

So now let's turn over to Slide 7 to talk about our 2017 financial results and our guidance for 2018. So operating earnings per share in 2017 were $5.59, marking the ninth consecutive year that we have exceeded our original guidance. And for the first time in company history, we exceeded $1 billion in operating earnings.

In 2018, tax reform is allowing us to reduce customer rates, which I'll detail a bit further in a minute. Tax reform will also benefit our shareholders. So we've increased our 2018 guidance by $0.10 per share versus the EPS guidance that we provided at the EEI Conference last November. This increased guidance to $5.78 is also the new base for our 5% to 7% earnings per share growth projections, and it is a 9% increase from the original 2017 EPS guidance that we provided a year ago. So we'll provide additional color on how the tax bills affect individual business units down the road. But that said, $0.10 per share -- the $0.10 per share increase in our guidance is wholly tied to the nonutility businesses in the early years of the plan. The utilities will begin to contribute to the increase in the latter part of the 5-year plan as the rate base funding of the utilities transitions from deferred taxes to a higher mix of equity and debt. So in the latter portion of our 5-year plan, EPS accretion from tax reform actually grows to -- in the range of $0.13 per share.

And then finally, as we mentioned at EEI, we will continue to target dividend increases of 7% through 2020. And the goal there is to get our payout ratio in line with our peer average, and then we'll continue to grow dividends in line with earnings after that.

So before I talk about the impacts of tax reform further, I want to highlight our efforts to maintain customer affordability. I do that on Slide 8. So as mentioned earlier, we're well positioned among our peers in our cost control efforts, and this is evidenced by our ability to continue to lower customer bills and business rates over the past 5 years. So average annual residential electric bills have decreased by 5% over the last 5 years. Gas bills, down 9% over the same period. Industrial electric rates have declined by 14% through 2017, while gas rates have decreased by 17%. So we've used our CI disciplines to drive these productivity increases, but we are also increasingly doing this work through technology deployment and the modernization of aging infrastructure. And then added to those, declining gas prices have certainly helped on the affordability front as well. So this focus, along with substantial savings from tax reform that will accrue to customers, will go a long way toward maintaining the customer affordability we want.

And speaking of tax reform, I'm going to move on to Slide 9 to provide a little more color on that topic. So plain and simple, tax reform is good for our customers, and it's good for our shareholders. So let me frame up how it affects each: First, this is a good thing for our utility customers. We plan to pass $190 million in savings onto our customers tied to the reduction in current tax expense. And then additionally, we anticipate refunding on the order of $70 million annually as a result of the remeasurement of deferred taxes at the 2 utilities in future rate proceedings. We're working closely with our regulators right now to determine how we'll flow these tax savings back to our customers.

So the second point I'll make on tax reform is that it's good for our shareholders. As I mentioned earlier, it's $0.10 accretive beginning immediately in 2018, and our 5% to 7% growth builds from this higher 2018 guidance. Operating earnings grow at our utilities over time. For our nonutility businesses, the tax benefit will accrue immediately to us on existing contracts. And I might mention that our existing contracts at GSP have very little exposure to lower FERC recourse rates. The exposure is on the order of $1 million, maybe $2 million.

With respect to future nonutility business contracts, every project and every negotiation has its own dynamics and includes a lot of variables. And depending on the nature of the competition, the tax benefit may accrue to us. If there's higher competition, it may accrue to our customer. Or as I expect will often be the case, we may share the upside that the tax changes have created.

With respect to the impact of tax reform on our balance sheet, we rolled out a plan at EEI last fall that called for an incremental $3 billion in capital, and that plan called for $500 million of equity over the next 3 years. So as a result of tax reform, we see the need for a modest additional $300 million. So when you put the 2 together, $800 million over the next 3 years. We're doing that because we're committed to maintaining balance sheet metrics that support our current credit ratings and maintaining balance sheet flexibility. That said, you know we always look for ways to minimize equity issuances by strengthening cash flows, and we've often been successful in doing just that in the past.

Well, I'm now going to turn things over to Peter Oleksiak to talk a bit more about our financial results. Peter, over to you.

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

Yes, thanks, Gerry. Before I get into the financials, just one comment on my Detroit Tigers. Never really an off-season in baseball. Even though there's snow on the ground here in Detroit, spring training is in full motion down in Florida, and there's -- hope springs eternal for my Tigers to beat the odds in 2018.

Getting with the financials, I'll start on Slide 11. As Gerry mentioned, 2017 came in strong, with earnings of $1 billion or $5.59 per share. For reference, our reported earnings were $1.1 billion or $6.32 per share. And you can find a detailed breakdown of the earnings by segment, including a reconciliation to GAAP reported earnings in the appendix. Overall, our growth segment operating earnings were $981 million or $5.48 per share.

Now let me touch on each segments in detail, starting at the top with our Electric Utility. DTE Electric's operating earnings for the year were $617 million or $5 million lower than 2016, primarily driven by the cooler weather and higher storm expenses, offset by the implementation of new rates. For a more detailed year-over-year earnings variance for our DTE Electric segment, you can find that in our appendix.

DTE Gas operating earnings were $149 million or $11 million higher than 2016. This increase was driven primarily by a new rate implementation, offset by higher depreciation expenses and property taxes related to capital.

Our Gas Storage and Pipeline business, operating earnings were $160 million, or $33 million higher than 2016. This increase was due to a full year of Link earnings and pipeline and gathering growth.

Operating earnings for the Power and Industrial businesses were $124 million or $29 million higher than 2016. This is primarily due to both incremental REF sites and volumes and higher steel-related earnings in 2017.

Rounding out our growth segments is the Corporate and Other segment, which is $10 million unfavorable compared to 2016, mainly due to higher interest expense.

Energy Trading had operating earnings of $20 million in 2017, down $5 million. Our trading company contributed $29 million of economic income in 2017, which is in line with target levels. The appendix contains our standard Energy Trading reconciliations on both economic and accounting performance. So overall, DTE earned $5.59 per share, $0.31 higher per share than 2016 EPS.

Now I'll switch over to 2018 guidance on Slide 12. Gerry mentioned, due to tax reform, we are increasing our operating earnings guidance from the early outlook we provided to you at EEI. There is no change in 2018 to the guidance for the 2 utilities. But over time, changes in our capital structure will increase earnings as more utility rate basis fund it with equity instead of deferred taxes. Thus, our utility equity will grow faster than rate base growth.

Our EPS guidance range is now $5.57 to $5.99, up from a range of $5.48 to $5.88. This $0.10 per share increase from the early outlook guidance midpoint is driven by our nonutility businesses.

And our GSP and P&I businesses see immediate earnings benefits from the lower tax rate from 35% to 21%, contributing an incremental $30 million at GSP and $15 million at P&I. Corporate and Other earnings will decrease by $26 million due to the lower tax shield on interest expense. Energy Trading will also benefit from tax reform, but we left the low end of the guidance the same due to how we conservatively plan and forecast the earnings for Energy Trading. Gerry mentioned earlier the $0.10 EPS accretion we see here in 2018 will grow to $0.13 by 2022, driven by utility earnings growth.

For the nonutilities, the $0.13 assumes tax benefits on existing contracts only. So if we share some of the tax benefits going forward and do deals that could help achieve our long-term nonutility growth targets or potentially provide upside. Our cash and capital guidance for 2018 can be found at the appendix.

Now I'd like to move to our balance sheet metrics on Slide 13. We have been consistent in our messaging over the years that maintaining a strong balance sheet is a priority. As one of the companies in our industry that benefits from tax reform, we're able to deliver EPS accretion, at the same time maintaining strong balance sheet metrics. One item that is benefiting cash in near term is the way that the AMT credits will work. We'll get a cash refund of about $300 million over 4 years, which partially offsets lower cash flows at the utilities.

At EEI, we announced $500 million of equity needs through 2020 to fund the increase in our investment plan. As Gerry described, as a result of tax reform, we will be issuing an additional $300 million over the next 3 years.

For the calendar year 2018, our plan is to issue $300 million of equity using internal mechanism. One way to think about it is that there's an additional $100 million that is due to the tax reform embedded within that $300 million.

We're committed to maintaining a strong balance sheet and will target FFO to debt of 18% to 19%, which is in line with metrics needed to support our current credit ratings. For the next several years, our pension will be fully funded, which creates some additional flexibility in our FFO-to-debt targets and keeps us well within the range of our current ratings. We look for ways to limit the amount of equity needed over the next 3 years. But under any outcome, tax reform is good for utility customers and good for shareholders.

I'd like to turn over to Jerry Norcia, who'll go over the long-term plan for producing this earnings and dividend growth.

Gerardo Norcia - *DTE Energy Company - President and COO*

Thank you, Peter. Those of you who have listened to our calls in the past have heard us talk about the transformation of our utility assets over time, a transformation that aims to produce excellent customer outcomes while also achieving substantially higher productivity levels. This will occur over the next 10 years and will be driven by significant investments in infrastructure for our customers. We are defining customer operational productivity goals to guide this transformation. And as Gerry mentioned earlier, we filed a Certificate of Necessity with the MPSC to build an 1,100 megawatt natural gas-fired power plant. That plant, along with renewable investments, will backfill the retirement of the 3 coal plants in the early 2020s. The nearly $1 billion project is scheduled to break ground in 2019 and will create hundreds of Michigan jobs during construction. Natural gas-fired plants will be an important complement to our renewable power investments in the decades ahead as natural gas offers an affordable, abundant, low-carbon domestic fuel source and is a reliable 24/7 power source for our electric customers. We're also planning to construct up to 4,000 megawatts of additional renewable energy capacity over time. The next major renewable investment for both wind farms will occur in 2018 and 2020. In fact, we have just finalized our plans for a $260 million wind investment this year.

At our electric company, we'll also continue to invest heavily in grid hardening and grid automation. As the infrastructure ages, there is an ongoing need to invest in modernizing the system. As we invest in the distribution system, we will be very focused on ensuring affordability for our customers, and we will do this through substantial productivity increases over the next decade.

At DTE Gas, we continue to focus on accelerating the replacement of our aging cast iron and unprotected steel pipe. In our last gas rate case, we proposed accelerating from a 25-year main renewal cycle to a 15-year cycle. At the same time, we continue to work to automate our gas meters and move them outside to reduce costs. Finally, we will continue to invest in pipeline integrity to harden the system and ensure a very high standard of public safety.

Now I'll move on to the nonutility businesses on Slide 16. As Gerry mentioned, we had many accomplishments at our nonutility businesses last year. At Gas Storage and Pipelines, much of our focus over the next few years will center on expanding our 2 newest growth platforms: NEXUS and the Link Pipeline. In 2017, we saw NEXUS Pipeline construction advancing and are on track for a late third quarter in-service date. We are progressing on pipe construction, right-of-away clearing, compressor station work and some horizontal directional drills this winter. In 2018, we are seeing continued progress of both NEXUS and Link. NEXUS is finalizing agreements to construct laterals to 2 new large industrial customers. We also told you late last year that we're in discussions with several producers about NEXUS capacity. The discussions continue to advance, and we are now exchanging proposals with producers to fill additional open capacity, giving us great confidence on our plan for this asset.

We continue to be pleased with the interest in NEXUS as well as the construction milestones we are achieving. We consistently said that the intensity of discussions around the remaining NEXUS capacity ratcheted up as the pipe moved into construction, and that's what we're seeing play out. Since we are under strict confidentiality agreements on these deals, we won't be able to provide any additional details at this point. As the deals become final, we will provide more information.

So moving on to our Link asset. We recently doubled capacity with an existing customer at an attractive rate. At our Bluestone asset in Pennsylvania, we achieved a 1 Bcf per day delivery capacity milestone in 2017. It's pretty exciting given that this pipeline started with a 0.3 Bcf per day capacity. We're expanding by an additional 0.1 Bcf per day in 2018.

We also have a newly signed precedent agreement with APV Renaissance for a new lateral pipeline to connect to their power plant. So all in all, I feel very good about the progress we've made at our GSP business, and I continue to feel we are on track to achieve our future goals.

Now I'll talk about progress at our Power and Industrial business on Slide 17. We have already talked about the new projects that we originated in 2017. In November at EEI, we told you that we needed to originate $45 million of new growth by 2022, and that was to achieve an income target of $65 million in 2022. $15 million, or 1/3 of that growth, was originated last year, including a state-of-the-art central energy plant and 2 renewable natural gas projects that Gerry mentioned. We also feel we have a good line of sight on the next $15 million in 2018, and we are well advanced with that with projects in late-stage discussions. So we could have 2/3 of that '22 growth target originated by the end of this year.

Tax reform may also help with this P&I growth, given that we may share the benefit with our customers on future projects. Back in November, we also told you about 5 cogeneration sites we are in advanced discussions with as well as 4 renewable natural gas projects that we are pursuing. While I'm pleased to tell you that we are finalizing negotiations on those new RNG projects, we are also firming up agreements for our new large-scale energy project. Given this start to 2018 and the fact that we have additional projects, I feel good about how P&I is positioned for the future growth.

Now I'll turn over to Slide 18 to wrap up. Once again, our strong 2017 extended our track record of exceeding original guidance. We're one of the companies in our industry who -- for whom tax reform provides benefits for our customers while also benefiting investors. We increased our 2018 operating EPS guidance by -- midpoint by $0.10 per share, which will serve as a new base for our 5% to 7% operating EPS growth target through 2022. Strength of our utilities and the growth at our nonutility businesses and a strong balance sheet, along with an annualized dividend growth target of 7%, gives me confidence that we will continue to deliver premium shareholder returns.

And with that, I'd like to thank everyone for joining us this morning. So Alecia, you can open up the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We'll go first to Julien Dumoulin-Smith of Bank of America Merrill Lynch.

Unidentified Analyst

It's Josephine here. Just a few questions here this morning. First, on the utility side. As you're thinking about the upcoming RFP and the 5-year distribution plan, are there any additional CapEx opportunities that could develop from that? And then secondly, on -- are there any regulatory mechanisms that you're looking for under that plan to ensure more concurrent recovery of the spend?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

So I'll start with the distribution plan. We are working very closely with the Public Service Commission staff right now. In fact, we're wrapping up a process, where we've been laying out the distribution system needs over the next 5 years. It's been a really healthy, open process. And I think what that is going to do is essentially lay the logic for the capital expenditures that we have in the plan that we've laid out for you. And then on the IRP front, I think the IRP is consistent with what we have said before that we're going to retire -- if you look over the next 5 years or so, retire those 2 coal plants. We need this gas plant to backfill those. We will continue to add renewables, both up through 2021 when the state target is 15%, but really beyond that as well. I fully expect that we'll continue to add additional renewables as the price on those continues to go down, and something our customers want us to do. So as far as additional CapEx, to be honest, I think the plan we've laid out is one that's got a healthy amount of work to renew our utility infrastructure, and that's what we're focused on executing.

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

I think -- this is Peter, Josephine. I think you were also asking about a recovery mechanism. This definitely will lay the potential groundwork for that and that we are in early discussions with the staff and the commission on that.

Unidentified Analyst

Awesome, great. And then on the P&I side, I'm curious if you could just give a little bit more color around the guidance increase. Is that just tax reform? Or does that also include volumetric and efficiency improvements?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

That is just tax reform.

Unidentified Analyst

Just tax reform, okay. Awesome. And then just one last question for GSP. As you're earning AFUDC on NEXUS right now and then the project moves into service, how are you thinking about the return profile in the project? Is there going to be any shift there in the earnings from NEXUS?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

The AFUDC is earned over time as you're doing your capital spend. So when you look at year-over-year, there's not going to be a -- kind of a material change between the 2. And as we put it in service, it gives them just the negotiator rates we have. And it's a healthy targeted cost of capital we have on the project right now. More than anything, it really lays the groundwork for additional expansions and investments around that platform.

Operator

We'll go next to Michael Weinstein of Crédit Suisse.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

Could you just remind us the extra equity -- the $300 million of incremental equity and in addition to the $500 million at EEI, what's the method for that? Is that a secondary? Or is it ATM?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

So we expect this year that it'll be internal mechanisms. We have capacity for about $300 million in internal mechanisms, although it varies year by year due to pension contributions and other things. But I think for the foreseeable future, we expect the vast majority would play out that way.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

Even the incremental amount, right?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Yes, yes.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

Okay, got you. And on the P&I side, I think you said that you'd be at 2/3 by the end of this year towards the goal?

Gerardo Norcia - *DTE Energy Company - President and COO*

That's correct. That's what we're expecting.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

What -- how long do you think it'll be before you actually finish completely?

Gerardo Norcia - *DTE Energy Company - President and COO*

Well, our forecast is to originate the $45 million by 2022. So I would say we are well in progress if -- with having 2/3 completed this year. And we'll have to revisit our targets the end of this year to see if there's any potential upside to that.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Yes. We've been -- gotten a fast start on it. So we said last year $45 million incremental needed, but we really think, at the end of this year, we'll be about $30 million into the $45 million, 2 years into the 5 years. So we'll just keep evaluating. If the market keeps offering us opportunities at that pace, as Jerry said, there could be some upside to what we talked about.

Michael Weinstein - *Crédit Suisse AG, Research Division - United States Utilities Analyst*

Okay. And just maybe you could just remind everybody like what your thoughts are on M&A these days. There's a lot of activity going on in your region, a lot of speculation. I'm just wondering what your thoughts are on M&A and the industry as a whole right now based on -- especially now with rates starting to rise and the valuation of the group as a whole. How do you view things?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

I view it pretty much the same way we always have. So we put a high bar out there for something that we think would actually be additive to what we think is a good, strong plan that we have. And so we look, but I think the characteristics you need are something that actually genuinely brings efficiency and cost reduction and maybe a handful that could do that. But as you know, you can't pay some of these really high premiums for that or that -- all of that is given away and more. So if we ever found one that was great for our customers through efficiency and could be done at low premium, maybe. But I'd just say we put a high bar out there for it. Don't see it at the forefront of our strategy right now.

Operator

We'll go next to Shar Pourreza of Guggenheim Partners.

Shahriar Pourreza - *Guggenheim Securities, LLC, Research Division - MD and Head of North American Power*

So you guys have never been capital constrained, right? Rates have always sort of been the governor. 3% reduction in rates from tax reform is somewhat material. So does this sort of provide an opportunity for you guys to accelerate some spending opportunities? Or asked differently, many utilities seem to be submitting plans to give back the tax savings through time, and they seem to be getting some preliminary support from the various commissioners. So why not retain some more of the savings and redeploy into sort of infrastructure needs since you sort of have the opportunity to do so?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

When you say retain some of the savings, what do you mean, Shar? Just so I'm clear on the question you're asking.

Shahriar Pourreza - *Guggenheim Securities, LLC, Research Division - MD and Head of North American Power*

Well, sort of subsidize additional opportunities to accelerate some of the infrastructure needs that you have.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Yes. I guess our reaction to this is that we're actually very happy to have this reduction go back to customers and to have it go back quickly. Because as you said, the thing that we worry most about as we go through this heavy infrastructure renewal cycle is keeping it affordable. I think the one thing that differentiates, actually, if you look back over time, companies that do well as you go through a heavy investment cycle versus those that don't is how they manage it for their customers, whether their customers and regulators remain supportive. And a lot of that is tied to how affordable it remains. And so when we saw this, it -- our reaction was good. It helps us achieve our targets for rates and rate levels. Now I think what, in the end, that's going to do is make feasible, in a way that works for everybody, the capital plan that we have laid out here over the next 5 years, which, as we've been saying, have some very heavy infrastructure investments embedded in it. So that's the way we're thinking about it. And when we generally get asked about upside as a result of this or trying to retain some of the tax savings for upside, that's not the way we're thinking about it. We're really thinking that it's a really helpful aid to the plan we have laid out in terms of keeping things affordable.

Shahriar Pourreza - *Guggenheim Securities, LLC, Research Division - MD and Head of North American Power*

Got it. So supportive of the plan, but not any way to accelerate the plan, okay. And then just on NEXUS. Jerry, I appreciate the sensitivity of the discussions. But on sort of the conversations you're having on the demand pull and supply push side, can you at least sort of disclose if these opportunities are enough to finally fully subscribe the pipe?

Gerardo Norcia - *DTE Energy Company - President and COO*

They certainly are. The size of the volumes that we're discussing would fill the pipe.

Shahriar Pourreza - *Guggenheim Securities, LLC, Research Division - MD and Head of North American Power*

Oversubscribe the pipe or just fill the pipe?

Gerardo Norcia - *DTE Energy Company - President and COO*

We'll start with fill it first.

Operator

We'll go next to Jonathan Arnold of Deutsche Bank.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

You just answered my first question, so moving to some of the P&I tax uplift. Could you just unpack the mechanics behind that a little bit, given the amount -- the sort of proportion of the earnings coming out of REF, just how we got -- where the uplift is coming from?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

Yes, Jonathan. This is Peter. We -- a portion of our facilities we have there, we essentially have sold down from a partnership perspective, so we have current kind of cash and earnings related to that. That's where the uplift is coming from. Now as we mentioned, the $0.10 accretion here will go to $0.13 to essentially that nonutility, and that REF will be replaced by utility accretion at the back half of the plan.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

So effectively, the incremental coming because you have to make up as the REF piece steps down?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

Right. So there is some protective benefit from REF just because -- with those facilities that we have partners with.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

Okay. So that's what's driving the uplift in 2018? It's in the accounting and the partnership?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

One way to think about it, by 2022, that is gone. But that's fully replaced and then some by utilities.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

Right. So instead of being $0.03 incremental, it's actually more than that?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

Yes.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

So it's -- just to add there, obviously, on the partnership positions, there's some tax savings. We also have other projects that are in REF, where there's obviously tax benefits as well on current contracts. And then the point Peter is making is we go through the transition Jerry Norcia was describing as we add RNG projects and industrial projects and so forth. On current projects of that type, we have benefit on future projects. I expect it'll be a shared benefit, where some of that goes to the customer and some of that comes to us.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

Okay, great. And then just another -- a little tax detail. So I think you mentioned that you've assumed the -- it's $190 million upfront for the reduced tax charge and then an assumption of $70 million a year on deferred excess flowing back. Can you just unpack that between protected and unprotected and then what sort of time frame you've assumed on each?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

Yes. There -- maybe I'll give you the broad context. There's going to be 3 different proceedings. One is going to be on the current, which is the $190 million you mentioned. So there'll be proceedings in terms of how do we give that back to customers. So maybe a little bit different for each of our utilities because where they're at in terms of the rate case cycles. There'll also be a portion on that current that will catch up from January 1. And then on the deferred, as you're talking about, there's going to be a separate proceeding second half of the year. There is -- good majority of it is to protect the depreciation, probably 2/3 of it. Some of it isn't, but we have history and precedents around all that being normalized. So we expect all that -- it could play out in the proceeding at the back half of this year.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

And then what are -- in your $70 million, what do you see about the 1/3 that's not protected?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

It'll be normalized as part of the $70 million. We have $1.4 billion roughly at electric company, $300 million at the gas. So combined, $1.7 billion that we're going to need to give back to customers over time. That includes both protected and unprotected.

Jonathan P. Arnold - *Deutsche Bank AG, Research Division - MD and Senior Equity Research Analyst*

1/3 of which is unprotected. And for the time being, you're assuming that that's also normalized. Am I getting that right?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

Yes. And there's precedents around that back in 1986 when we did this with the commission.

Operator

We'll go next to Paul Ridzon of KeyBanc.

Paul Thomas Ridzon - *KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst*

I think you just answered my question. But the $0.13 is inclusive of the $0.10 at unreg. Is that correct?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Correct. That's correct. So we get an immediate $0.10, and then a slow build to $0.13 as we play through the 5 years.

Paul Thomas Ridzon - *KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst*

It will build from $0.10 to $0.13?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Correct.

Paul Thomas Ridzon - *KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst*

And then looking forward, when you report first quarter earnings, if there's no resolution of tax issues at the commission, how should we think about you'll just -- at the utilities, just strip that out as like kind of reserved revenues?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

That is correct. It's a regulatory liability from an accounting perspective, so we'll be putting that in our balance sheet to get back to our customers through these various proceedings that I described earlier.

Operator

We'll go next to Steve Fleishman of Wolfe Research.

Steven Isaac Fleishman - *Wolfe Research, LLC - MD & Senior Utilities Analyst*

So first question, just in clarifying the growth rate guidance. The 5% to 7% off of the $5.78 in 2018, so that number obviously includes trading. So I assume you're kind of giving -- when you're giving that, you're including trading kind of throughout the period. If we want to exclude that, we just take that out and grow 5% to 7%?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

We do include it. So we're growing up the total number in trading a couple percent of our total so we're confident.

Steven Isaac Fleishman - *Wolfe Research, LLC - MD & Senior Utilities Analyst*

Okay. So I guess in -- it's a small thing, but in theory, since that -- you're probably not assuming that grows, then the businesses ex trading are probably growing a little quicker?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Could be or we might see a little growth in trading. I mean, when you do the math, it's a few million dollars, so it's -- it just doesn't swing much in the growth. So we're looking for them to do what they've done. It's $25 million to $30 million of cash a year that we can use to reduce equity. That's their role.

Steven Isaac Fleishman - *Wolfe Research, LLC - MD & Senior Utilities Analyst*

Okay. And then just to clarify, the bullet in the slide on tax on the improvement in the economics, future nonutility projects, maybe shared with customers, is this mainly in the P&I segment?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

I think it's both. If you think logically about it, every project has lots of variables that come into determining your return on capital. But one of them is competitive dynamics and how many opportunities they are competing for the opportunity. And so if there's low competition, presumably, the -- and you really are the one best suited to serve the need, you might have a higher share. If high competition, the share might be lower. And then I think a lot of cases that we play out in, we'll see a split of that value. So we've tried to be conservative and not play a lot of that future tax value on future projects into our projections. But I think we'll see it and will help us in our achievement.

Steven Isaac Fleishman - *Wolfe Research, LLC - MD & Senior Utilities Analyst*

But you're not talking to an impact on kind of current nonutility projects?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

The ones that are already existing and are in hand with negotiated contracts in place, we'll obviously get the benefit, yes.

Steven Isaac Fleishman - *Wolfe Research, LLC - MD & Senior Utilities Analyst*

Okay. And then can you just talk a little bit to the ALJ and your electric case? And I think they came out with like a 9.6% ROE, which was not only down a decent amount from where you've been, but also lower than CMS. Like, what is the explanation for that? And how are you feeling about the outcome?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

So we're in an active case, Steve, so I'm probably going to leave most of our commentary for that venue. But that said, if you've watched our ROE proceedings and our rate case proceedings over the years, it's not unusual to see positions out there that are lower than what we have or what we filed for. But when you step back from all of that, I feel we're going to get a constructive set of outcomes in our electric and gas cases and constructive on the ROE front that will support the plan we've put out for the year, so...

Steven Isaac Fleishman - *Wolfe Research, LLC - MD & Senior Utilities Analyst*

Okay. And then last question, just on -- in the midstream business. Just high level, maybe you could talk to trends that you're seeing. Obviously, we have a lot more gas production. We have demand increasing, but bottlenecks starting to get slowly get resolved. Just what are you thinking strategically next for the business? Are you worried about pricing and too much supply? Or do you still see like a lot of opportunity to grow the business?

Gerardo Norcia - *DTE Energy Company - President and COO*

Certainly. With our current slate of assets tied to the Marcellus and the Utica, we kind of see a world-class resource connected to very proximal markets on the East Coast as well as the Midwest. And the markets in Midwest, which is what our NEXUS Pipeline is pointed to, you're going to see a fundamental shift from coal use to natural gas use over time as these plants age out, as you can see from our own sort of plans for generation. So I see very strong supply growth as well as strong demand growth in the regions that we're going to serve with NEXUS. And I think that will bode well for additional bolt-on projects for NEXUS as well as our Link asset, which is already connected to the NEXUS. So I see a really strong story in our future. I think also, the evolution of the export market and the natural gas industry, I think, will be an outlet for what continues to be a growing supply of natural gas in North America. So overall, I feel our midstream business, with its sphere of influence, if you will, in the Great Lakes region, is well positioned to capture that growth, both supply and demand.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Steve, just to add on to that, if you go to our position in Pennsylvania, Bluestone and Millennium, we hit a record production level last year. And as we mentioned, we got pull for more there. Down on our Link assets, we just had a producer there double their position with us. And if you come up to NEXUS, one of the interesting things there is that I think in a region where output is growing rapidly, the producers are definitely scaling up operations there. NEXUS is, for the next couple of years, likely to be the only path out with any capacity. We're working to make sure that capacity doesn't exist for very long as we fill up the pipe, but we are an option out of the region -- or out of that zone right now as it scales up production.

Operator

We'll go next to Angie Storozynski of Macquarie.

Angieszka Anna Storozynski - *Macquarie Research - Head of US Utilities and Alternative Energy*

I actually wanted to follow up on NEXUS. So I heard your explanation. Now the contracts with industrial customers are for the -- to fill the existing capacity or for expansions of NEXUS?

Gerardo Norcia - *DTE Energy Company - President and COO*

They will be both.

Angieszka Anna Storozynski - *Macquarie Research - Head of US Utilities and Alternative Energy*

And can you give me a sense what type of industry this is that would be willing to sign contracts for -- from Continental Gas? Is it...

Gerardo Norcia - *DTE Energy Company - President and COO*

Angie, once we execute the agreements, I'd be happy to disclose that. But at this time, we can't.

Angieszka Anna Storozynski - *Macquarie Research - Head of US Utilities and Alternative Energy*

Okay. And so -- and separately on the drillers' demand for capacity on your pipe, it seems like Rover is still not fully subscribed. So -- and again, it seems like Rover's pricing is a little bit lower than yours. So what would be the advantage for a driller to choose your pipe versus Rover?

Gerardo Norcia - *DTE Energy Company - President and COO*

Well, let me be clear, our -- Rover's rates are not lower than ours. And I think you and I have had this conversation before that our rates are very competitive with Rover, so we're happy with our position in the market that way. And in addition to that, we've got much greater significant -- or much more significant market access along the pipeline route. We've got 13 interconnects that we are building immediately. And all of those interconnects with large demand centers are already starting to play into some of the discussions that we're having with counterparties. So we feel very good about filling this pipe.

Angieszka Anna Storozynski - *Macquarie Research - Head of US Utilities and Alternative Energy*

Okay. And then lastly, when you show us the net income range for '18 for the GSP segment, does it account for any incremental long-term contract? Or is basically the delta year-over-year largely filled by short-term contracts?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Are you asking about long-term contracts on NEXUS or other pipes?

Angieszka Anna Storozynski - *Macquarie Research - Head of US Utilities and Alternative Energy*

In other pipes as well. I mean, will they materialize between now and the end of the year and to contribute to '18 net income?

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

So NEXUS not materially since it goes into service so late in the year. So it's really -- that's really not relevant for '18. And the other pipes do have growing positions. So for example, we mentioned Link and a growing position there. Now that will take a little time to come into, but could contribute some. We're going to be growing over at Bluestone. So the projections we have for both '18 and future years are taking that sort of growth in those sorts of contracts into account. But the contracts on NEXUS just -- there isn't enough time in '18 for those to really be material (inaudible) third quarter.

Operator

We'll go to Charles Fishman of Morningstar.

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

I am assuming that, since I didn't hear any comments toward this, the timing of the REF phaseouts has not changed with tax reform.

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

It has not. It has not.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

True.

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

Okay, that is what I assumed. And then the second question on P&I. Getting to 2/3 of your way to your goal by the end of year, is that -- did you say that's an expansion of the Ford agreement? Or is that a new project you intend to announce?

Peter B. Oleksiak - *DTE Energy Company - Senior VP & CFO*

So these are -- the one project that we're looking to finalize agreement -- we're very close to finalizing an agreement is an RNG project currently, and we are looking at other industrial energy projects in the region.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

We have a number of cogen projects, for example. And one of the discussions with an industrial counterparty is, I guess we'll just say, very late-stage development. So (inaudible) the likelihood of them going forward is high. We were a year ago with Ford at this point is the way that project feels. So we've got one of those. We've got an RNG that's -- that we think about finalized. And then more of each of those behind those new projects.

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

But the -- so there is a project in the mix and there's still these projects coming out that are similar to Ford, where you build a cogeneration facility for a big industrial complex?

Gerardo Norcia - *DTE Energy Company - President and COO*

That's correct.

Operator

That is all the time we have for questions. At this time, I would like to turn the call back over to our speakers for any additional or closing comments.

Gerard M. Anderson - *DTE Energy Company - Chairman & CEO*

Well, look, thanks very much for joining us this morning. Hope you feel that the way we wrapped up '17 was positive. And as I said at the outset, I feel great about our position for 2018. I think we're lined up for another really good year this year, and we look forward to describing all of that to you in future discussions. Thanks for joining us.

Operator

That does conclude our conference for today. We thank you for your participation.
