

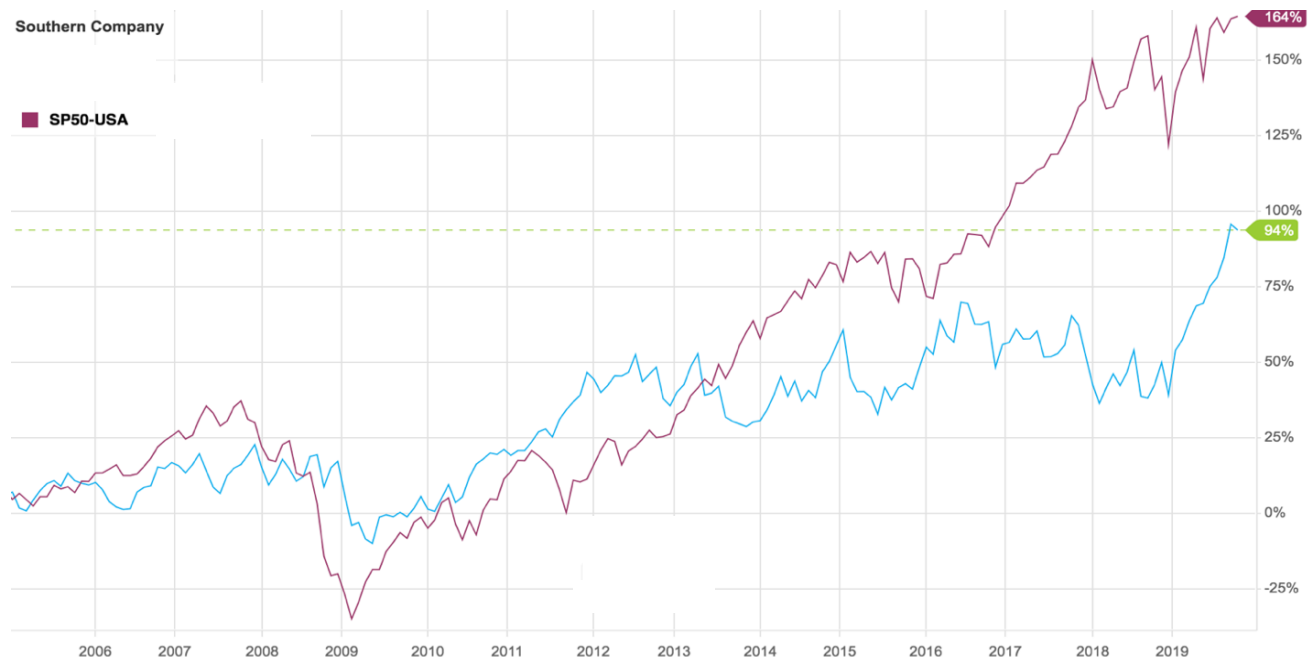
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Sector: Energy & Utilities



Business Background

The Southern Company is a utility holding company and one of the largest energy providers in the United States. It serves a customer base of 9 million people through its operating segments such as the traditional electric operating companies, Southern Power, Southern Company Gas, and other businesses. The traditional electric utilities refer to vertically integrated utilities that own generation, transmission and distribution facilities, and supplies electric services in the states of Alabama, Georgia, and Mississippi. The Southern Power segment constructs, acquires, owns, and manages generation assets such as renewable energy projects and sells electricity in the wholesale market in 12 states. The Southern Company Gas segment is the largest component of Southern Companies Gas business and it distributes natural gas through utilities in the states of Illinois, Georgia, Virginia, Tennessee. Other businesses of Southern Company include PowerSecure, Southern Holdings, and Southern Linc. They provide energy solutions and digital wireless communications for use by Southern Company and its subsidiaries and also to the public. The company was founded on November 9, 1945 and is headquartered in Atlanta, Georgia.

Stock Chart



Southern Company is a regulated-utility company that is a defensive stock. The company provides high dividends to its stockholders and has been overall stable in the business cycle over the past few years. The stock has been performing well since last year and it is currently around \$60, and it is anticipated to perform better in the future decades.

Recommendation

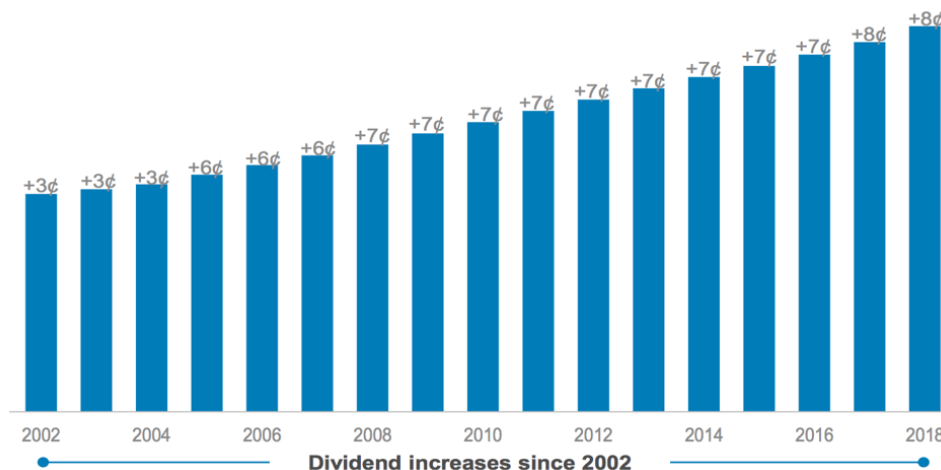
We recommend a **BUY** for Southern Company's stock at \$61.14 due to the following reasons:

- This large cap firm has a monopolistic advantage in the states that they service, serving a total of 9 million customers in the United States.
- Southern Company is a defensive stock with a low beta of 0.26 as they are less volatile to the market. Hence, it reduces the risk of losing value in the portfolio by owning the stock.
- The company is highly diversified by owning and operating several segments, which generate a mix of energy and other subsidies that run other businesses that are related to energy.
- Given that the company is regulated by the government and the projects that the company is undertaking such as nuclear energy generation, will help the company to generate steady earnings and dividends growth in the next coming years.
- Southern Company is the only utility company that is building a nuclear power plant in the United States. This makes it unique from other utility companies.
- By setting efficiency targets, Southern Company is able to complete their nuclear project in time and start working towards their next goal.
- Rising of renewable energy due to climate change will positively impact Southern Company's growth in the future as the company involves in generating renewable energy.
- The company has outperformed its sector with its outstanding growth of a revenue growth rate of 154.8% YoY increase in 2018, due to the high demand in electricity sales. Southern Company has an attractive dividend yield of 4.3% with a solid payment history compared to its industry's dividend yield of 3%.

Investment Thesis

Defensive Sector and High Dividend Yield

The economy is in a bull market for more than ten years since the financial crisis in 2008 and many economists and analysts have predicted that a recession is bound to happen. Therefore, it is safe to invest in stock in the utility sector because they will remain stable in a recession. Holding Southern Company as a utility stock in the portfolio can help with reducing the risk of potential loss in the future. For instance, in the last financial crisis, Southern Company's shares fell 12% from the peak, compared to S&P 500 companies which have declined by 42.3% between July 2007 and July 2009. On the other hand, Southern Company pays relatively high dividends to its shareholders compared to other utility companies. The dividend yield for Southern Company has been increasing since 2002 and is currently at a 4.3%. The beta of the stock is 0.26, which makes the investment of Southern Company stock to be more conservative, which means investing in a lower-risk security. At the same time, the company pays high dividends due to their relative stable cash flows.



Leading Utility Company in U.S. Electric and Gas

Ever since Southern Company has completed the acquisition of AGL Resources, it has made itself a leading United States energy company. These two utilities companies that have outstanding performance by providing world-class customer service to invent America's future energy providing services have merged and thus making Southern Company's energy infrastructure to be more equipped. Also, being the second-largest utility company in the United States, Southern Company total operations include nearly 200,000 miles of electric transmissions and distribution lines, which generate a capacity of approximately 44,000 megawatts. The company also has a market cap of \$64.38 billion, showing Southern Company with the benefit of having a large customer base. Southern Company has helped the economic and community development in the United States. It has approximately 30,000 employees to run its operations and in the last five years, the company has brought an average of 18,000 new jobs and \$6 billion in capital investment every year to the Southeastern US.

Low-carbon Future Plan

Southern Company has set the aim of cutting nearly all its greenhouse gas emissions by 2050 and they are planning to cut 50% of its emissions across all operation by 2030 from 2008 levels. Currently, the company has successfully decreased its carbon emissions by 36% from 2007 levels and the power generation for coal production has declined by 60%. Furthermore, the plan includes cutting methane emissions from the natural gas distribution company operations to 1% or less of total natural gas production. By 2022, Southern Company expects to add more renewables production capacity upon the completion of its Vogtle Nuclear 3 and 4 units. The new units will be the first new-generation nuclear facility in the United States in 30 years and the first to use the Westinghouse AP1000 advanced pressurized water technology. The company continually improve and maintain its diversified energy portfolio that includes generation of renewable energy such as hydroelectric, biomass, solar, wind and energy efficiency programs to reduce carbon emissions.

Risks

Allowed Return Changes

Southern Company, controlling multiple state utilities, is exposed to the risk of the allowed return for states they operate changing. The allowed return is set by utilities commissions in each state, this rate controls what how much revenue the company can generate based on the operating costs, depreciation, and value of assets. If the commissions decide to change the rate allowed the revenue for Southern Company can increase or decrease. Since the changes from the commissions are hard to predict, this can be a risk for Southern Company. Southern Company operates in multiple states meaning they are somewhat protected from potential revenue drops as a commission from one state can only affect a minority portion of the company.

Complications on Vogtle Plant Construction

The Vogtle Plant 3 and 4 is a nuclear power plant being constructed in Georgia. The plant is owned by 4 separate power companies with Georgia Power, a subsidiary of Southern Company, being the largest stakeholder at 45.7% ownership. Vogtle 3 is scheduled to be completed in November 2021 and Vogtle 4 is scheduled to be completed in 2022. With the date still being a full two years out, the potential for delays is a large risk for this company. In 2018, the company recognized over a billion in losses on plants in construction because of the delays and increased estimated completion cost. If construction were to be delayed or overbudget again, Southern Company would cause a face regulatory, financial, and execution risk. However, the risk will be minimized if the Vogtle plant is able to complete its operations without any additional material delays or cost increase.

Clean Energy Regulations

As our world becomes more aware of the dangers of carbon emissions, and continues to move towards clean energy, it is possible for energy companies to fall behind the regulations. The biggest reason it is taking a long time for companies to switch over to clean energy is because of the large upfront costs of implementing new plants and renewable generation. In an extreme case, if the United States Environmental Protection Agency were to require completely renewable generation by 2025, Southern Company would have to spend an enormous sum of money to comply and could put themselves under some credit risk. Therefore, unpredicted changes in regulations can be a risk for the Southern Company.

Valuation

For our Valuation, we used a two stage Dividend Discount Model (DDM), which considers two stages of growth, combined with a multiples model based on book value. In our DDM, we used 3% growth for 3 years for the first stage and 2% for the second stage in perpetuity. We chose to use 3% as a conservative estimate for the growth rate of the model as compared to the latest 3 years dividend growth rate of 3.4%. This model gave us a target price of \$121.18. Our multiples approach used the book value per share of the company multiplied by the industry average for price to book ratio. This gave us a target price of \$55.01. To combine the two models, we put 65% of the weight in the multiples approach and 35% in the DDM, which left us with a final target price of \$78.16 representing a potential upside of 27.8%.

Peer Analysis

Company Name	Price	Mkt Cap (M)	PE (NTM)	PEG (NTM)	ROE (%)	EPS YoY (%)	Sales (M)
Southern Company	\$61.14	\$63,905.50	19.5	4.5	16.9	158.3	\$23,615.0
Duke Energy Corporation	\$95.35	\$69,472.10	18.6	4.3	7.4	-13.8	\$24,521.0
Entergy Corporation	\$118.15	\$23,491.70	21.4	9.7	10.5	103.0	\$11,069.0
CenterPoint Energy, Inc.	\$28.64	\$14,383.60	16.5	3.2	9.3	-82.2	\$10,486.0
American Electric Power Company, Inc.	\$94.14	\$46,485.90	21.6	3.9	10.3	0.4	\$16,167.0
Exelon Corporation	\$44.67	\$43,395.80	14.4	6.0	7.3	-47.8	\$36,094.0

Management

- Southern Company's board members have a diverse perspective to the technological advancements and evolving dynamics that are reshaping the energy industry.

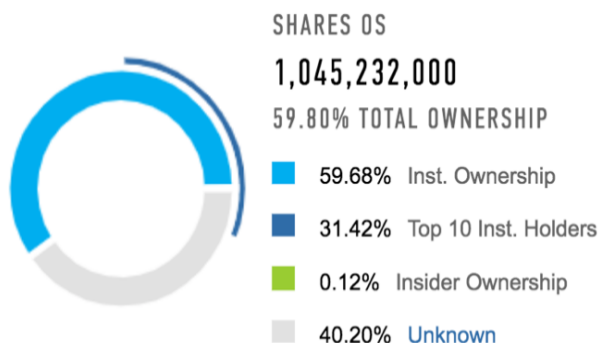
CEO- Thomas A. Fanning

- Thomas A. Fanning is a businessperson who has been the head of 5 different companies and currently holds the position of Chairman, President and CEO of Southern Company.

CFO- Andrew W. Evans

- Andrew W. Evans is the CFO and Executive Vice President at the Southern Co. and CEO at Georgia Natural Gas Co. (a subsidiary of the Southern Co.) and Chairman, President & CEO for Southern Company Gas LLC. He received an undergraduate degree from Emory University.

Ownership Summary



Holder	%OS	Mkt Val (M)
The Vanguard Group, Inc.	8.27	\$5,284
SSgA Funds Management, Inc.	5.08	\$3,245
BlackRock Fund Advisors	4.99	\$3,191
T. Rowe Price Associates, Inc. (Investment Management)	3.35	\$2,142
Franklin Advisers, Inc.	2.88	\$1,843