

Commonwealth Energy System *weekly* **Highlights**

Topics

- Tucker Anthony's investors report on COM/Energy stock
- More Summerfest photos on back

Informing you about our energy industry.

week in review...

August 24, 1994



Some of the COM/Electric volunteer crew: (from left, front to back) Stanley Jasinski, Energy Account Rep.; Kevin Harnett, Professional Engineer; Vivian Medeiros, Supervisor Accounts Payable; Bob Lawrence, Professional Engineer; Ellie Quadros, Administrative Coordinator; Russ Wright, President & Chief Operating Officer; (right front to back) David Medeiros (Vivian's husband); Kimberlee Wiley (daughter of Jeanne Wiley); Peg Johnson, Administrative Secretary; Barbara Trahan, Secretary Public Communications.

COM/Electric Shows Community Pride At New Bedford Summerfest

Tens of thousands came to the 1994 Great New Bedford Summerfest for the food, the crafts displays and the carnival rides. About 70 COM/Electric employees came to volunteer their time to help make the annual civic event a success.

Sponsored by the Greater New Bedford Area Chamber of Commerce, Summerfest is a way of showcasing the best of the New Bedford community. The 100,000 visitors who came to the harborside festivities the weekend of July 29th enjoyed a variety of activities, including a whaleboat race, tugboat muster and even a

chance to climb aboard the HMS Bounty - the actual ship used in the 1962 film, "Mutiny On The Bounty."

Of course, the main attraction of Summerfest is the fresh-off-the-boat seafood. And where the seafood was being served you could find an orange COM/Electric tee-shirt. Event chairman, Steve Beauregard, told the New Bedford Standard Times that the many Commonwealth Electric volunteers had done everything for the festival, "from serving food to cleaning tables."

Lisa Sughrue, manager of Summerfest, made a point of thanking COM/Electric coordinator Barbara Trahan for securing so many volunteers.

"COM/Electric's involvement is certainly appreciated," she said. "It made the festival run smoothly again this year."

Update-Buy

Commonwealth Energy System (CES/NYSE)

July 27, 1994

DJIA: 3735.04
S&P 500: 453.11
Prices as of 7/22/94 close.

Current Price:	\$40 1/2	QUARTERLY EARNINGS PER SHARE (Loss):			
52-Week Range:	\$50 1/2-\$39 1/4	Qtr.	12/93A	12/94E	12/95E
Shares Outstd.:	10.4 Million	1Q	\$2.34	\$2.68A	\$2.51
Market Capitalization:	\$421.2 Million	2Q	0.18	0.15	0.23
Daily Avg. Trading Vol.:	4,920	3Q	0.52	0.47	0.54
Dividend/Yield:	\$3.00/7.4%	4Q	1.33	1.22	1.35
Book Value/Share:	\$34.50	Yr.	\$4.37	\$4.52	\$4.62
3-Yr. EPS Growth:	4%	P/E	9.3	9.0	8.8
12- to 15-Mo. Target:	\$46-\$48				

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Commonwealth Energy System is a small-cap electric and gas utility holding company serving mostly residential and commercial customers in central and eastern Massachusetts, including Cape Cod. Power, which is based primarily on oil (40%) and nuclear fuel (28%), is supplied by a wholesale subsidiary, Canal Electric, and retail subsidiaries Commonwealth Electric and Cambridge Electric. Commonwealth Gas, which owns its own gas storage facilities, provides gas service to 227,000 customers. Nuclear power is derived from the company's 2.5% to 4.5% interests in the three Yankee Atomic plants and a 3.5% ownership in the Seabrook plant.

We are maintaining our Buy recommendation on Commonwealth Energy because of expectations for continued earnings improvement, a safe and attractive yield of about 7.4%, a low 66% payout ratio, exceptionally strong cash flow of about \$10 per share and an improving balance sheet. Even considering the emerging competitive environment for utilities, we believe Commonwealth Energy's stock is undervalued. Our 12- to 15-month price target is \$46-\$48.

- **Dividend increase.** As we anticipated, with improved earnings prospects, a 2.7% common dividend increase was announced for the current quarter. This is the first increase in four years and brings the annualized rate to \$3 per share.
- **Cost-cutting initiatives.** An aggressive cost-cutting program at the company's high-cost Commonwealth Electric subsidiary (the Canal and Cambridge Electric subsidiaries are below-average-cost power producers) has already reduced O&M costs almost 13% this year, dropping power cost by 2%. The full impact of last year's downsizing and cost reduction initiatives should be realized later this year, helping to improve the company's competitive market position. The latter will be further enhanced with the likely buyout of some high-cost, state-mandated power supply contracts with independents.
- **Effects of weather.** Because of the stock's thin float and low number of outstanding shares, weather factors have a significant leverage effect on EPS.

Key Investment Considerations

Earnings got off to a good start this year as an extremely cold winter helped boost first quarter EPS 14% to \$2.68 from \$2.34 last year. Given normal weather over the balance of this year and only a nominal improvement in the regional economy, 1994 EPS should increase to the \$4.50-\$4.55 range based on the net effect of an expected 1.5% increase in KWH sales, ongoing cost reductions, scheduled recovery of lost revenues from conservation programs and the balance of a \$7.2 million Cambridge Electric rate increase that went into effect in June 1993. Our preliminary 1995 EPS estimate of \$4.62 assumes normal weather and that Commonwealth Energy continues to achieve a 13% ROE.

The stock has a safe dividend, in our opinion, of \$3 per share, or a 7.4% yield. It is currently selling below the industry's average market-to-book, price-to-earnings and price-to-cash flow ratios (see page 4). The relatively high yield and below-average financial ratios are traceable in part to the overall depressed market, concern over the company's competitive market position and prior lack of dividend growth. The latter has been remedied and the former should improve as the year wears on.

Earnings improvements and strong cash flow have helped reduce long-term debt at March 31 from 56% last year to 54% this year. The balance sheet has also benefited from a reduction in short-term debt.

At \$10 per share, internal cash generation is exceptionally strong. With capital spending and common dividend requirements of about \$100 million for the next several years, Commonwealth Energy should need little net new external financing since cash from net income and depreciation will also be about \$100 million (see adjacent table).

Although Commonwealth Energy is, in aggregate, an above-average-cost power producer in the Northeast region, only 6% of total electric revenues are derived from industrial customers. In addition, its 1993 system average industrial rates of \$0.091/KWH, though marginally above the region's average rates, were below Boston Edison's (BSE/NYSE - \$26 1/2) rates of \$0.093. Also, Commonwealth Energy (Canal Electric) is selling wholesale power to Boston Edison at about \$0.03/KWH. Commonwealth Energy's competitive position is clearly not as bad as it is made out to be. Also, many of Commonwealth Energy's larger industrial customers are already receiving below-average economic incentive rates, which will tend to keep them on the system. Continued cost-cutting and business development initiatives in the Cape Cod area, where a high-cost transmission system serves a low volume of residential sales and keeps average rates high, should help improve relative power costs over the next few years.

Valuation

With any improvement in the overall market, the stock should respond well to the combination of higher earnings prospects, resumed dividend growth, strong cash flow, an improving balance sheet and progress on reducing power costs. In our opinion, it is likely that the market price will move up to reflect the industry's average financial ratios more closely. This would move the stock to the \$46 to \$48 range, indicating a total return potential of 20% to 25% over the next 12 to 15 months.



COM/Gas' Don Triner, Manager Customer Services NB/Ply, wore a COM/Electric t-shirt in the spirit of the system.



Fresh seafood, anyone? Vivian Medeiros, Supervisor Accounts Payable offers service with a smile.



Peg Johnson, Administrative Secretary, works the crowd while Russ Wright's daughter, Becky, helps prepare food in the background.



Joe DeMello, Lineman 3rd Class NB and his wife Mary

COM/Energy Stock and Vanguard Accounts

Item	1/1/92	12/31/92	12/31/93	8/5/94	% Change YTD
CES	\$39 ½	\$42 ⅞	\$46 ¼	\$39 ⅞	-13.8
MMR-P	4.9%	3.2%	3.0%	4.2%	N/A
STCorp	\$10.97	\$10.87	\$10.90	\$10.51	-3.6
IdxExt	\$15.77*	\$17.35*	\$19.43*	\$19.11	-1.6
IntlGr	\$10.22*	\$9.41*	\$13.51*	\$14.27	+5.6
Welltn	\$18.68	\$19.16	\$20.40	\$20.18	-1.0
WindsII	\$14.84	\$15.91	\$17.04	\$17.00	-0.2

*Fund only available to Commonwealth Energy System employees since 10/1/93
Price on 10/1/93 of IdxExt was \$19.58 and IntlGr was \$12.11

Please contact Eric de Lacoste, extension 4246, with any comments or suggestions



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