factiva

THE WALL STREET JOURNAL.

HD **Heard on the Street / Financial Analysis and Commentary**

WC 1,443 words
PD 10 October 2008
SN The Wall Street Journal
SC J
NGC The Wall Street Journal - Print and Online
GC CTGWSJ
PG C12
LA English
CY (Copyright (c) 2008, Dow Jones & Company, Inc.)

LP Still Some Energy Left in Market

Power companies that sell electricity in deregulated markets have been among the hardest hit by the stock-market selloff. So hard, in fact, that they are selling for a fraction of their inherent value.

TD The market capitalization of Reliant Energy Inc. has fallen by about 75% over the past month, to $1.2 billion. It had net debt of about $2.5 billion as of June 30. But the replacement cost of its generating plants suggests an enterprise value of $9.6 billion to $12.1 billion, says Samuel Brothwell, analyst at Wachovia.

A similar calculation by Citigroup in early October found four other companies -- Dynegy Inc., Mirant Corp., NRG Energy Inc. and Calpine Corp. -- also were selling for a fraction of the value of their power plants alone.

Some companies, such as Allegheny Energy Inc. and Sempra Energy, which also own regulated utilities with predictable earnings, have still fallen sharply in the recent market slide.

The energy sector -- the third-biggest borrower after government and **finance** -- relies on debt to **finance** at least half the cost of building power plants. For that reason, credit turmoil dealt a blow to the sector by creating uncertainty about the cost and availability of capital. As stocks slide, it becomes less attractive and more difficult to issue equity as a source of capital.

Shares in Houston-based Dynegy, which owns more than 18,000 megawatts of power plants in deregulated markets, have lost half their value in the past month and 77% since May. One reason is that falling natural-**gas** prices -- off 45% since early summer -- have depressed wholesale power prices and lowered revenue projections. That is especially painful for firms such as Dynegy that don't sell much of their expected output under multiyear contracts.

Unlike banks, many of which hold hard-to-value mortgage assets, energy companies own power plants that make an essential commodity, electricity. Assuming firms get through the crunch, slumping values now may lay the groundwork for a sharp recovery.

That's because current tough conditions, while making life difficult for those needing debt to **finance** existing projects, also choke off investment for new plants. At some point in the future, an economic rebound should push up demand -- forcing existing plants to run harder and prices to go up, allowing them to generate stronger profits.

Of course, one notable buyer has already identified a bargain in the sector: billionaire investor Warren Buffett.

His Berkshire Hathaway Inc. stepped in last month to rescue Constellation Energy Group Inc. for $4.7 billion. Constellation owns all or part of three nuclear generating stations, **utility**Baltimore **Gas** and Electric Co., assorted other power plants and an electricity-retailing business. Mr. Buffett's deal gives him the whole thing for less than half what one new reactor is expected to cost.

-- Rebecca Smith

2008 Factiva, Inc. All rights reserved.

Sears Shares Seem Ripe for a Reduction

It's time for a markdown sale at Sears.

Despite steadily declining same-store sales and plunging profitability over the past 18 months, Sears's stock is defying gravity. But a looming recession is likely to bring the retailer back to earth.

Even after coming way off its highs of last year, Sears's stock is trading at the nosebleed valuation of about 26 times this year's expected earnings. In comparison, discount retailers such as Wal-Mart Stores and Costco Wholesale -- both of which reported higher same-store sales in September, even as consumers deserted other stores -- are trading in the mid-to-high teens. Not to mention lower-profile retailers like TJX Cos., whose chains draw brand-conscious consumers looking for a bargain, which is trading at a multiple of about 11.

Part of the reason for the anomaly could be Sears's inclusion on the no-short-sale list; indeed, Thursday, after the ban expired, Sears fell sharply. Sears also benefits from a relatively small float, as several loyal investors have stuck by controlling shareholder Eddie Lampert. And the company has been steadily buying back stock, even as cash generation has slumped.

At some point, though, the faith in Mr. Lampert displayed by these investors may start to crumble. Recessions are the ultimate in Darwinian exercises for retailers. Every time there's a severe economic downturn, a smattering of big and small retail chains go bankrupt. Recent months have already seen a handful of specialty chains file for Chapter 11 bankruptcy protection, including Steve & Barry's, Linens 'n Things and Mervyn's. Others, like electronics chain Circuit City and drugstore operation Rite Aid Corp., face serious challenges. Sears says it has more than enough liquidity. But an extended downturn will test that.

-- Martin Peers

Malone Swallows a Loss

It isn't just Ukrainian tycoons and bank executives who are getting burned by the stock-market crash.

Cable-TV magnate John Malone, who made a fortune with companies such as Tele-Communications Inc. and Liberty Media, may have come under some pressure.

The Liberty chairman sold 4.5 million shares of his Liberty Capital A tracking stock back to the company for $11 a share Tuesday, according to a Liberty filing.

What raised eyebrows is that the sale came just three months after Mr. Malone paid more than $14 each for 6.6 million of the shares.

The sale has little effect on his voting control as the A shares are low-voting.

But it's a little embarrassing, given the likelihood that he got hit with a margin call.

A government filing in July noted that Mr. Malone had pledged a portion of his Liberty holdings to Bank of America "in connection with a line of credit."

As of Tuesday the pledged stock was down 21% to $75.6 million from early July; it has fallen even further since.

Mr. Malone likely has plenty of other assets he could have sold to raise $50 million, including some of the huge chunks of land he has acquired in recent years.

But he might have decided that a roughly $15 million loss on Liberty Capital was preferable to, and less painful than, selling anything else.

-- Martin Peers

Eyes Turn

To One Bank

As Barometer

2008 Factiva, Inc. All rights reserved.

Morgan Stanley has become a critical test case.

Panic has reached fever pitch. Morgan Stanley's shares have come under severe pressure, including a 26% drop Thursday, as investors bet it's the latest Wall Street firm to get into trouble.

But if Morgan Stanley pulls through, it would represent an important milestone in the search for a stock-market bottom. At some point, a high-profile financial firm will survive fear-stoked selling. When that happens, it might abate.

In theory, Morgan Stanley looks OK. It has marked down bad assets aggressively, and management has responded to the crisis with realism. After changing its banking status, Morgan Stanley has access to wider Federal Reserve funding.

Also, the bank's capital ratios got a boost upon agreeing to a $9 billion capital infusion from Mitsubishi UFJ Financial Group, scheduled to close Tuesday. Given the circumstances, Mitsubishi has an incentive to walk away. But it isn't the sort of bank that reneges on deal terms. Doing so would be a risk as its recent acquisition of a U.S. commercial bank means it needs to be on good terms with the Fed.

Granted, all that might not help Morgan Stanley, if clients leave and trading counterparties pull back and demand higher collateral.

To squash the fear, a private-sector solution would be best -- for example, if Mitsubishi itself offered up a big credit line to Morgan Stanley. Or if another bank stepped up to buy the firm outright.

If not, the government might yet need to step in. And if that led to a punitive outcome for shareholders, the market would take aim at the next firm.

-- Peter Eavis

Overheard

Creed is good.

Wall Streeters, having already thrown themselves on the mercy of the Federal Reserve, are appealing to an even higher power.

Attendance at lunchtime services at Trinity Church, the Gothic landmark that looms over the western entrance to the Street, is up sharply in recent weeks.

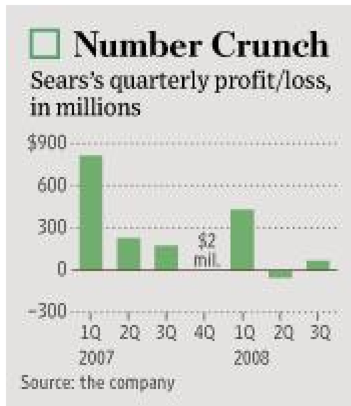
After Thursday's stock-market rout, expect standing room only.

With Citigroup no longer trying to block Wells Fargo's purchase of Wachovia, Wells has a greater chance of completing the deal.

One problem: To support the purchase Wells previously said it needed to raise $20 billion.

Good luck with that, given that Bank of America, a much bigger institution, struggled hard to raise half that earlier this week.

2008 Factiva, Inc. All rights reserved.



License this article from Dow Jones Reprint Service

CO rlnrsc : Reliant Energy Inc | tringl : Dynegy Inc | ccred : Citigroup Inc | funcp : Wachovia Corp

IN i16 : Electricity/Gas Utilities | i1 : Energy | i13 : Crude Oil/Natural Gas | i162 : Gas Utilities | i814 : Banking | i81402 : Commercial Banking | ibnk : Banking/Credit

NS c1521 : Analyst Comment/Recommendation | c181 : Acquisitions/Mergers/Takeovers | ccat : Corporate/Industrial News | ciprof : Industry Profile | c15 : Performance | c152 : Earnings Projections | c18 : Ownership Changes | ncat : Content Types | nfact : Factiva Filters | nfce : FC&E Exclusion Filter | nfcpin : FC&E Industry News Filter

RE eurz : European Countries/Regions | usa : United States | usca : United States - California | usco : United States - Colorado | use : Northeast U.S. | usga : United States - Georgia | usil : United States - Illinois | usmd : United States - Maryland | usmn : United States - Minnesota | usnc : United States - North Carolina | usny : United States - New York | ustx : United States - Texas | namz : North American Countries/Regions | usc : Midwest U.S. | uss : Southern U.S. | usw : Western U.S.

IPC BKG CMR DJCB EWR NRG PIC CYC FCL NND UTI HST MIM TPT

PUB Dow Jones & Company, Inc.

AN Document J000000020081010e4aa0003g

2008 Factiva, Inc. All rights reserved.