



COMPANY UPDATE / TARGET CHANGE ESTIMATE CHANGE

Key Metrics

NWN - NYSE - as of	2/24/17	\$61.40
Price Target		\$50.00
52-Week Range	\$48.90 -	\$66.17
Shares Outstanding (mm)		28.6
Market Cap. (\$mm)		\$1,754.2
1-Mo. Average Daily Volume		112,741
Institutional Ownership		63.8%
LT Debt/Total Capital	Q4'16	45.8%
ROE	TTM	7.3%
Book Value / Share	Q4'16	\$30.16
Price / Book Value		2.0x
Dividend Yield		3.1%
LTM EBITDA Margin		-

EPS FY 12/31

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	*\$1.40	--	\$1.35	--	--
2Q	\$0.07	--	\$0.03	--	--
3Q	(\$0.29)	--	(\$0.28)	--	--
4Q	\$1.00	--	\$1.03	--	--
Year	\$2.19	\$2.17	\$2.13	\$2.30	\$2.25
P/E	28.0x		28.8x		27.3x

*Adjusted for special items

Net Operating Revenue (\$MM, excludes cost of sales)

		Prior	Current	Prior	Current
	2016A	2017E	2017E	2018E	2018E
1Q	\$147	--	\$148	--	--
2Q	\$78	--	\$79	--	--
3Q	\$59	--	\$61	--	--
4Q	\$130	--	\$135	--	--
Year	\$415	\$419	\$423	\$430	\$433

Company Description: NW Natural is a natural gas distribution company headquartered in Portland, Oregon, and has been in business nearly 160 years. It serves 725,000+ residential and business customers in Oregon and southwest Washington. The company also provides natural gas storage and related transportation services. It is the largest independent natural gas utility in the Pacific Northwest.

Natural Gas Utilities

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Northwest Natural Gas Co.

NWN – NYSE – Underperform-2

Mixed Q4'16 Caps Transition Year at NWN.

Investment Highlights

- NWN reported Q4'16 EPS of \$1.00, down \$0.08 yr/yr and below our estimate for \$1.02; consensus called for \$1.04. FY 2016 adj. EPS slipped 4.5% to \$2.19, as expense growth offset higher utility margin and a rebound year for the Storage segment.
- NWN initiated 2017 EPS guidance at \$2.05-\$2.25; current consensus is for \$2.30. Easy comps could make weather constructive this year, but greater shares outstanding will be a modest headwind.
- Net operating revenue (NOR) grew 4.8% on the full year, due in part to a cosmetic accounting change. Utility gross margin grew just 0.6% in 2016.
- Utility customers rose 1.5% yr/yr exiting 2016, an escalation from prior years, but not yet sufficient, in our view, to be a standalone catalyst for the stock.
- Operations and Maintenance (O&M) expense growth accelerated across 2016, rising 10.2% in 2H. We expect most reflation of the cost structure is complete, but still model above-trend growth in 1H'17.
- Representing a true upside surprise for us, gas storage operations contributed EPS of \$0.16 in 2016, rising from \$0.01 in 2015 and (\$0.01) in 2014. Construction of the Mist expansion should be mostly complete this year, and in-service for the 2018-2019 heating season.
- NWN continues to operate with an interim CFO, although we expect a permanent announcement within the next couple of months.
- Our FY 2017E EPS slips \$0.04 to \$2.13, but remains within guidance; our 2018E EPS slips \$0.05 to \$2.25.
- We are reiterating our Underperform rating, but raise our 1-yr target by \$1 to \$50. At \$50, NWN would trade at ~23.5x our 2017E EPS, roughly in line with our gas utility industry comp group.

Note Important Disclosures on Pages 5-6
Note Analyst Certification on Page 5

ADDITIONAL DISCUSSION—MULTIPLE ITEMS

We view 2016 as a transition year for Northwest Natural. From an operational standpoint, the company substantially concluded the lingering items from the 2012 general rate case (final charge should have occurred in Q1'16), and effectively pivoted efforts toward growth, perhaps most notably beginning construction of the N. Mist expansion project. Reflating the cost structure and employee base flows along these thematic lines as well, as NWN looks to shed some temporary measures implemented in the last few years. A rebound at the Storage segment came as a welcome surprise, although with interest savings contributing to the yr/yr upside, we do not necessarily extrapolate the same level of growth into 2017/2018.

In response to our query on the conference call this morning, CEO David Anderson noted that the company should have an announcement regarding a permanent CFO in relatively short order. Brody Wilson, who was most recently the firm's Chief Accounting Officer, continues to serve in the role of interim-CFO. In our view, Mr. Wilson is the likely front runner to be named the permanent successor to Gregory Hazelton, who departed in September of last year, based primarily on our view that he offers the best continuity for the position that has seen relatively high turnover across the past several years.

NWN continues to prepare for a base rate case filing in Oregon, per prepared remarks from management this morning. Timing guidance for a filing to occur (with high probability) 'within the next year or so' is relatively inexact; however, it does bring about the possibility for new rates within our typical 1-2 year investment time horizon. A base filing in Washington could follow a case in Oregon by about a year. As investors begin to handicap the rate case process, we remind interested parties that OR holds a 10-month (fully litigated) rate case process, by statute, with the provision for interim rate relief if the case stretches past ideal conclusion.

SUITABILITY

We assign NWN a suitability rating of '2.' A complete description of our suitability scale is on page 5. Size versus peers across the Utility sector and a relatively narrow geographic focus keep Northwest Natural well below our '1' suitability rating. Sector-appropriate leverage, a consistent history of capital return and a highly regulated business mix keep NWN a bit above our more aggressive '3' rating.

CONSIDERATIONS AND RISKS

Utility operations are weather sensitive. Warmer weather can lead to lower total margin from lower volumes of natural gas sold or transported, while extremely cold weather may lead to conservation by customers in order to reduce consumption.

Gas utilities face competition from alternative fuels. In the industrial market, many customers have the capability of using both natural gas as well as another source of energy. Increases in the price of natural gas can negatively impact a competitive position by decreasing the price benefits of natural gas to the end user. The cost of natural gas from non-domestic sources may play a greater role in establishing the market price of natural gas in the future.

Gas utilities are subject to regulation at the federal and state levels. Regulatory commissions and policies vary from state to state, and have a significant bearing on the profitability of gas utilities.

Our Suitability rating is 2 on a 1-to-4 scale (1 = most conservative, 4 = most aggressive).

Additional information is available upon request.

Northwest Natural Gas (NWN)

Income Statement	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Operating Revenues:													
Operating Revenue	\$754,037	\$723,791	\$255,529	\$99,183	\$87,727	\$233,528	\$675,967						
Cost of Gas	365,490	327,305	108,411	20,871	28,264	103,042	260,588						
Revenue Tax	-	-	-	-	-	-	-						
Net Operating Revenue	388,547	396,486	147,118	78,312	59,463	130,486	415,379	147,840	79,400	61,270	134,610	423,120	433,370
Operating Expenses:													
O & M	136,982	157,521	38,939	35,962	34,870	40,203	149,974	38,370	37,680	35,570	41,010	152,630	154,250
Enviro Remediation		3,513	5,029	1,893	1,191	5,185	13,298	5,030	1,890	1,190	5,190	13,300	13,300
General Tax	29,407	30,281	8,684	7,438	7,211	7,205	30,538	8,730	7,540	7,430	7,430	31,130	31,820
D & A	79,193	80,923	20,394	20,413	20,628	20,854	82,289	21,130	21,160	21,360	21,550	85,200	87,770
Total Operating Expense	245,582	272,238	73,046	65,706	63,900	73,447	276,099	73,260	68,270	65,550	75,180	282,260	287,140
Operating Income	142,965	124,248	74,072	12,606	(4,437)	57,039	139,280	74,580	11,130	(4,280)	59,430	140,860	146,230
%	36.8%	31.3%	50.3%	16.1%	-7.5%	43.7%	33.5%	50.4%	14.0%	-7.0%	44.1%	33.3%	33.7%
Other Inc / (Exp)	1,933	7,747	(2,309)	513	652	601	(543)	10	513	652	601	1,776	1,770
Interest--Net of Captzd	44,563	42,539	9,736	9,718	9,729	9,945	39,128	10,380	10,160	10,070	10,250	40,860	40,280
Pre-tax Income	100,335	89,456	62,027	3,401	(13,514)	47,695	99,609	64,210	1,483	(13,698)	49,781	101,776	107,720
Income Tax	41,643	35,753	25,386	1,382	(5,474)	19,420	40,714	25,363	586	(5,616)	20,210	40,543	42,964
Net Income	58,692	53,703	36,641	2,019	(8,040)	28,275	58,895	38,847	897	(8,082)	29,571	61,233	64,756
Average shares outstanding (FD)	27,223	27,417	27,560	27,550	27,554	28,202	27,427	28,708	28,716	28,724	28,732	28,718	28,751
EPS	\$2.16	\$1.96	\$1.33	\$0.07	(\$0.29)	\$1.00	\$2.11	\$1.35	\$0.03	(\$0.28)	\$1.03	\$2.13	\$2.25
Adjusted EPS		\$2.29	\$1.40				\$2.19						
Dividends	\$1.845	\$1.863	\$0.4675	\$0.4675	\$0.4675	\$0.4700	\$1.873	\$0.4700	\$0.4700	\$0.4700	\$0.4725	\$1.883	\$1.893
Rate of Change Analysis:													
Net Operating Revenue	0.9%	2.0%	8.2%	2.9%	3.8%	2.6%	4.8%	0.5%	1.4%	3.0%	3.2%	1.9%	2.4%
O&M Expense	0.3%	15.0%	-28.0%	1.8%	8.9%	11.5%	-4.8%	-1.5%	4.8%	2.0%	2.0%	1.8%	1.1%
Operating income	0.2%	-13.1%	39.8%	-2.4%	136.9%	-5.3%	12.1%	0.7%	-11.7%	-3.5%	4.2%	1.1%	3.8%
EPS	-3.7%	6.1%	2.2%	-8.6%	19.4%	-7.3%	-4.5%	-3.5%	-57.4%	-3.6%	2.7%	-2.5%	5.6%
EBITDA	1.6%	-7.6%	29.2%	-0.4%	-12.3%	-3.2%	8.0%	1.3%	-2.2%	5.5%	4.0%	2.0%	3.5%
Margin Analysis:													
O&M/Net Op Rev (NOR)	35.3%	39.7%	26.5%	45.9%	58.6%	30.8%	36.1%	26.0%	47.5%	58.1%	30.5%	36.1%	35.6%
General Tax / NOR	7.6%	7.6%	5.9%	9.5%	12.1%	5.5%	7.4%	5.9%	9.5%	12.1%	5.5%	7.4%	7.3%
Op Income / NOR	36.8%	31.3%	50.3%	16.1%	-7.5%	43.7%	33.5%	50.4%	14.0%	-7.0%	44.1%	33.3%	33.7%
Tax Rate	41.5%	40.0%	40.9%	40.6%	40.5%	40.7%	40.9%	39.5%	39.5%	41.0%	40.6%	39.8%	39.9%
Net Income / NOR	15.1%	13.5%	24.9%	2.6%	-13.5%	21.7%	14.2%	26.3%	1.1%	-13.2%	22.0%	14.5%	14.9%
			*\$3.3MM pre-tax charge; \$0.07/sh AT for reg disallowance				Adj EPS guidance \$2.05-\$2.25					EPS guidance \$2.05-\$2.25	Expect Mist storage for PG&E to be on-line 2018 2019 heating season; \$18MM investment

Source: Company reports and Hilliard Lyons estimates

Northwest Natural Gas (NWN)

Summary Balance Sheet (000s)	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Cash	\$9,534	\$4,211	\$5,218	\$5,463	\$6,230	\$3,521	\$3,521	\$9,880	\$9,000	\$5,010	\$17,530	\$17,530	\$16,870
A/R	69,818	68,228	69,066	23,353	25,506	66,700	66,700	70,450	23,820	26,020	68,030	68,030	69,390
Inventory	77,832	70,868	60,581	66,171	67,470	54,129	54,129	60,580	66,170	67,470	54,130	54,130	54,130
Other CA	205,376	188,756	137,335	107,073	111,379	163,703	163,703	140,080	109,210	113,610	166,980	166,980	170,320
Total Current Assets	362,560	332,063	272,200	202,060	210,585	288,053	288,053	280,990	208,200	212,110	306,670	306,670	310,710
Net PP&E	2,121,593	2,182,663	2,196,667	2,214,452	2,233,862	2,260,900	2,260,900	2,276,770	2,292,610	2,308,250	2,326,700	2,326,700	2,398,930
Regulatory Assets	368,908	370,711	351,390	344,969	341,188	357,530	357,530	361,930	355,320	351,420	368,260	368,260	379,310
Other	211,884	191,255	181,776	181,663	174,249	173,318	173,318	185,410	185,300	177,730	176,780	176,780	180,320
Total Assets	\$3,064,945	\$3,076,692	\$3,002,033	\$2,943,144	\$2,959,884	\$3,079,801	\$3,079,801	\$3,105,100	\$3,041,430	\$3,049,510	\$3,178,410	\$3,178,410	\$3,269,270
ST Debt	234,700	270,035	164,900	152,800	194,900	53,300	53,300	33,300	23,300	58,300	153,300	153,300	193,300
A/P	91,366	73,219	57,407	57,756	55,933	85,664	85,664	54,540	54,870	53,140	81,380	81,380	77,310
CP of LTD	40,000	25,000	24,980	24,987	64,994	39,989	39,989	40,000	40,000	22,000	22,000	22,000	30,000.00
Other CL	103,344	109,460	114,936	78,090	86,877	95,564	95,564	117,230	79,650	88,610	97,480	97,480	99,430
Total Current Liabilities	469,410	477,714	362,223	313,633	402,704	274,517	274,517	245,070	197,820	222,050	354,160	354,160	400,040
LTD	621,700	576,700	569,745	570,045	530,219	679,334	679,334	679,320	679,320	697,320	697,320	697,320	689,320
Regulatory Liabilities	317,205	339,287	346,761	341,259	342,143	349,319	349,319	349,320	349,320	349,320	349,320	349,320	349,320
Def Tax Liabilities	530,965	530,021	550,731	554,400	544,575	557,085	557,085	556,240	559,940	550,020	562,660	562,660	568,290
Other	358,344	371,998	365,618	363,808	361,041	369,049	369,049	369,270	367,450	364,650	372,740	372,740	376,470
Shareholders' Equity	767,321	780,972	806,955	799,999	779,202	850,497	850,497	905,880	887,580	866,150	842,210	842,210	885,830
Total Liab & SE	\$3,064,945	\$3,076,692	\$3,002,033	\$2,943,144	\$2,959,884	\$3,079,801	\$3,079,801	\$3,105,100	\$3,041,430	\$3,049,510	\$3,178,410	\$3,178,410	\$3,269,270
Summary Cash Flow (000s)	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Net Income	\$58,692	\$53,703	\$36,641	\$2,019	(\$8,040)	\$28,275	\$58,895	\$38,850	\$900	(\$8,080)	\$29,570	\$61,230	\$64,760
D&A	79,193	80,923	20,394	20,413	20,628	20,854	82,289	21,130	21,160	21,360	21,550	85,200	87,770
(Inc) / Dec in Wrk Cap.	(21,930)	13,143	50,534	33,888	(794)	(41,759)	41,869	3,964	34,660	(670)	(92,920)	(54,970)	(6,370)
Other Operating	99,702	36,919	38,569	(2,898)	(4,955)	8,378	39,094	12,000	2,000	(2,000)	12,000	24,000	24,000
Operating CF	215,657	184,688	146,138	53,422	6,839	15,748	222,147	75,944	58,720	10,610	(29,800)	115,460	170,160
Cap Ex	(120,092)	(118,320)	(30,054)	(32,099)	(35,958)	(41,400)	(139,511)	(37,000)	(37,000)	(37,000)	(40,000)	(151,000)	(160,000)
Utility Gas Reserves	(26,798)	(1,549)	-	-	-	-	-	-	-	-	-	-	-
Other Investing	2,567	4,571	24	2,429	415	14	2,882	-	-	-	-	-	-
Investing CF	(144,323)	(115,298)	(30,030)	(29,670)	(35,543)	(41,386)	(136,629)	(37,000)	(37,000)	(37,000)	(40,000)	(151,000)	(160,000)
Change in ST Debt	46,500	35,335	(105,135)	(12,100)	42,100	(141,600)	(216,735)	(20,000)	(10,000)	35,000	95,000	100,000	40,000
LTD Proceeds	-	-	-	-	-	150,000	150,000	-	-	40,000	-	40,000	20,000
LTD (Retired)	(80,000)	(60,000)	-	-	-	(25,000)	(25,000)	-	-	(40,000)	-	(40,000)	(20,000)
Stock Issued--Net	8,986	3,875	1,999	2,333	500	55,290	60,122	500	500	500	500	2,000	2,000
Dividends	(50,093)	(49,243)	(12,823)	(12,854)	(12,879)	(12,952)	(51,508)	(13,490)	(13,500)	(13,500)	(13,580)	(54,070)	(54,410)
Other Financing	3,336	(4,680)	(39)	11	(250)	(2,809)	(3,087)	400	400	400	400	1,600	1,600
Financing CF	(71,271)	(71,271)	(115,998)	(22,610)	29,471	22,929	(86,208)	(32,590)	(22,600)	22,400	82,320	49,530	(10,810)
Net Cash Flow	63	(1,881)	110	1,142	767	(2,709)	(690)	6,354	(880)	(3,990)	12,520	13,990	(650)
EBITDA	\$222,158	\$205,171	\$94,466	\$33,019	\$16,191	\$77,893	\$221,569	\$95,710	\$32,290	\$17,080	\$80,980	\$226,060	\$234,000
EV / TTM EBITDA	9.1x	9.7x	9.2x	10.5x	10.0x	10.8x	10.8x	11.1x	11.1x	11.1x	10.9x	10.9x	10.5x
Selected Financial Statistics	FY'14	FY'15	Q1'16	Q2'16	Q3'16	Q4'16	FY'16	Q1'17E	Q2'17E	Q3'17E	Q4'17E	FY'17E	FY'18E
Book Value	\$28.11	\$28.43	\$29.28	\$29.04	\$28.28	\$30.16	\$30.16	\$31.55	\$30.91	\$30.15	\$29.31	\$29.31	\$30.80
Price / Book	1.8x	1.8x	1.8x	2.2x	2.1x	2.0x	2.0x	1.9x	2.0x	2.0x	2.1x	2.1x	2.0x
LT Debt / Total Capital	46.3%	43.5%	42.4%	42.7%	43.3%	45.8%	45.8%	44.3%	44.8%	45.4%	46.1%	46.1%	44.8%
Total Net Debt / Total Capital	53.6%	52.6%	48.3%	48.1%	50.1%	47.5%	47.5%	45.1%	45.3%	47.1%	50.4%	50.4%	50.3%
ROE (TTM)	7.7%	6.9%	7.9%	7.9%	7.7%	7.3%	7.3%	7.4%	7.1%	7.0%	7.0%	7.0%	7.2%

Source: Company reports and Hilliard Lyons estimates

Analyst Certification

I, Spencer E. Joyce, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

Important Disclosures

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

Suitability Ratings

- 1** - A large cap, core holding with a solid history
- 2** - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks
- 3** - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage
- 4** - Speculative, due to small size, inconsistent profitability, erratic revenues, volatility, low trading volume or a narrow customer or product base

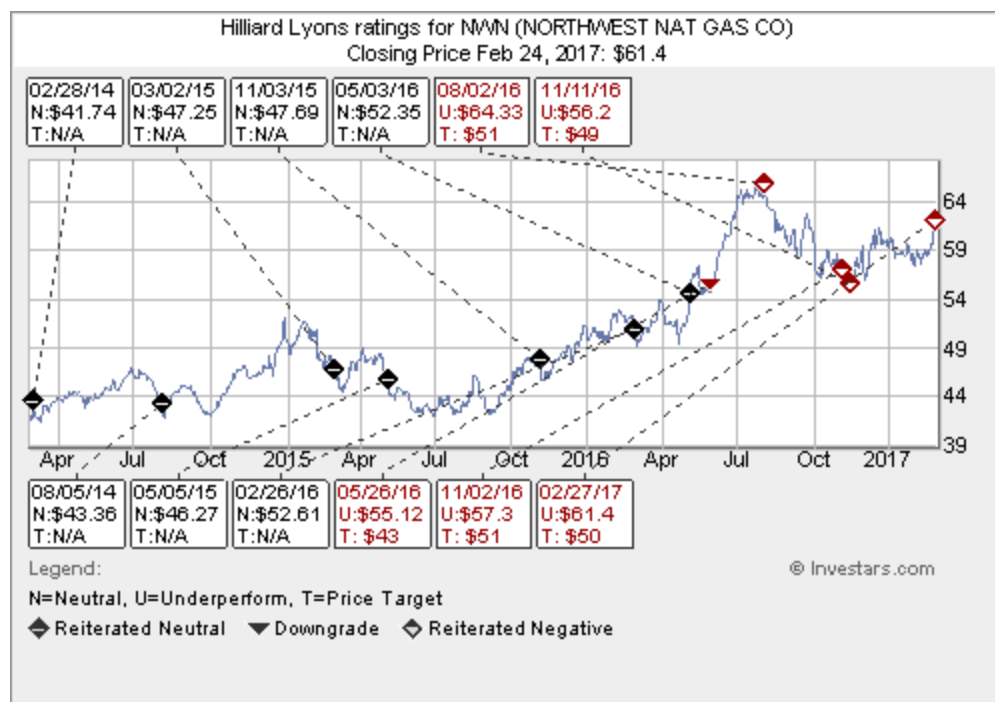
Investment Ratings

Buy - We believe the stock has significant total return potential in the coming 12 months.

Long-term Buy - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

Neutral - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

Underperform - We believe the stock is vulnerable to a price setback in the next 12 months.



Rating	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	36	30%	17%	83%
Hold/Neutral	76	62%	7%	93%
Sell	10	8%	0%	100%

As of 6 February 2017

Other Disclosures

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