https://www.wsj.com/articles/popular-hedge-fund-bet-on-pg-e-upended-by-californias-deadliest-fire-11547477495

MARKETS

# PG&E Was a Hedge-Fund Darling. That Bet Flopped.

Since the November fire, PG&E shares have plunged, challenging the idea that utilities are a safe bet

PG&E workers taking apart broken power lines in November after the Camp Fire, California's deadliest and most destructive wildfire, ripped through Paradise, Calif. **PHOTO:** JOEL ANGEL JUAREZ/ZUMA PRESS

*By Juliet Chung and Nicole Friedman*

Updated Jan. 14, 2019 6:54 p.m. ET

Utilities have long been considered ultrasafe bets. But PG&E Corp.'s PCG **-52.36%** ▼ announcement Monday that it will file for bankruptcy is teaching investors that isn't always true.

The Baupost Group LLC, Viking Global Investors LP and BlueMountain Capital Management LLC were among the hedge funds that snapped up shares of PG&E PCG **-52.36%** ▼ Corp. during the third quarter of 2018, just before the deadliest wildfire in California history triggered an existential crisis for the state's largest utility.

That crisis entered a new phase Monday when PG&E said that it intends to seek chapter 11 bankruptcy protection by the end of the month due to more than $30 billion it faces related to its role in sparking deadly California wildfires in 2017 and 2018. That sent its shares down 52%.

Shares have now fallen 83% since the fire began on Nov. 8 and bonds are down 25%. The price of PG&E bonds due in 2034 fell about 8% Monday, according to MarketAxess.

The decline of PG&E reinforces the notion that no industry is insulated from unexpected volatility that can create huge losses for investors. Insolvency means PG&E stockholders could have their shares wiped out and bondholders could also be hit.

In recent weeks, some hedge funds have exited their losing PG&E trades, while others continue to buy or look for other ways to profit, people familiar with the matter said. Seth Klarman's $30 billion Baupost, which posted a loss on its PG&E position last year, has spoken to several insurance companies about potentially buying their claims against PG&E, people familiar with the hedge fund said.

Investment funds including Avenue Capital Group, Elliott Management Corp. and King Street Capital Management LP on Monday were buying PG&E bonds, according to people familiar with the firms. Several traders said they expected a bankruptcy settlement would repay bondholders in full, based partly on expectations that PG&E would settle its wildfire liabilities for less than expected. As a regulated utility, PG&E also still has cash flow to pay creditors, and analysts said Monday's closing share price of $8.38 reflects the potential for some kind of rescue by California lawmakers or regulators leading up to the expected bankruptcy filing.

PG&E said in a securities filing Monday that it concluded state assistance would take years—too long to avoid a bankruptcy proceeding. California Gov. Gavin Newsom, who took office this month, said he would work with state lawmakers "throughout the months ahead" on a solution but didn't say he would try to prevent a bankruptcy filing.

Utilities are typically favored by individual investors seeking safe, dividend-producing stocks. A string of fires in California starting in 2017 challenged that assumption as the infernos devastated communities and killed dozens. PG&E suspended dividend payments in December 2017.

Unlike in most states, California utilities can be found liable if their equipment contributed to a fire, regardless of negligence.

This isn't the first time PG&E has caused volatility for shareholders. PG&E's utility unit filed for bankruptcy in April 2001 following an electricity crisis in California. Its share price fell below $7 but later recovered.

Some hedge funds began buying into PG&E in late 2017 after the wine-country fires introduced uncertainty around the company and drove down its stock price. By the third quarter of 2018—the most recent quarter for which such data is available—PG&E was one of the hedge-fund industry's most widely held stocks. About 19% of PG&E stock was held by hedge funds at the end of the third quarter, up from 3.4% a year earlier, according to FactSet.

Discussions about PG&E became a fixture of "idea dinners," where hedge-fund managers discuss companies and markets, traders said. Many of the funds were betting on possible

MORE

- PG&E Prepares for Bankruptcy Amid Wildfire Fallout
- CEO of PG&E Steps Down
- After Sparking at Least 1,500 California Fires, PG&E Faces Collapse

legislative and regulatory action that could limit PG&E's wildfire liabilities, they said. Some viewed the risk of another major wildfire in 2018 as low or believed the state would bail out the utility if a major blaze occurred, traders said.

Citigroup Inc. and political analysis firms Capstone LLC and Washington Analysis LLC organized trips to Northern California for clients to meet with legislators and former regulators, people familiar with the matter said. Hedge funds and other investment firms say such meetings can be informative, for example by providing a glimpse into how decision makers think.

"The regulators were getting involved, the legislators were going to get involved, and so we got involved," Washington Analysis President Leslie Alperstein said. The firm typically doesn't focus on utility companies.

The bets came under pressure in recent months as PG&E shares swung wildly. When a California Public Utilities Commission official said on a conference call hosted by Bank of America Corp. in November that the agency doesn't want PG&E to go bankrupt, shares soared. Last week, the stock plunged 28% due to credit downgrades and continued uncertainty.

> Some big investors, like Viking, exited their PG&E positions at a loss before Monday's bankruptcy announcement, according to people familiar with the matter.

Baupost has remained active on PG&E. Its interest in potentially buying insurers' claims against PG&E could offset its soured bet on the utility's shares. The Boston hedge fund last year bought CSAA Insurance Group's claims to recover from PG&E roughly $1 billion CSAA has paid out to policyholders following wildfires in 2017, people familiar with the transaction said. Baupost paid up to 35 cents on the dollar, some of the people said. AAA insurer CSAA said it sold its 2017 wildfire claims to an investment-management firm without naming the firm.

Other firms kept buying shares prior to Monday's announcement. A BlueMountain spokesman said the firm increased its position in the fourth quarter. The $19 billion multistrategy firm lost money on PG&E last year but thinks the company's wildfire liabilities will ultimately prove far smaller than analysts believe, people familiar with the firm said.

Knighthead Capital Management LLC, a $3 billion investor that specializes in distressed assets, lost money on PG&E last year when it removed a hedge on its stock position, people familiar with the fund said. It has bought this year as share prices slumped further, one of the people said.


Flames burning near power lines in Montecito, Calif., in December 2017. **PHOTO:** MIKE ELIASON/ASSOCIATED PRESS

One small hedge fund said it has made a paper profit off PG&E: Liver more Partners LLC, a hedge fund outside Chicago that manages less than $100 million, bet against PG&E's stock price in the fourth quarter when it was trading around $25 and added to its short position recently, partly because of downgrades to the company's credit last week, founder David Neuhauser said.

"November got me digging," Mr. Neuhauser said of the fire that started on Nov. 8 and the questions it raised about PG&E's liabilities. "The key is being nimble, and sometime you just got to go with instinct."

*—Sam Goldfarb contributed to this article.*

**Write to** Juliet Chung at juliet.chung@wsj.com and Nicole Friedman at nicole.friedman@wsj.com