

FINAL TRANSCRIPT

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PNY - Q3 2008 Piedmont Natural Gas Earnings Conference Call

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CORPORATE PARTICIPANTS

John Sutphin

Piedmont Natural Gas - Manager of Finance and IR

Tom Skains

Piedmont Natural Gas - Chairman, President, CEO

Dave Dzuricky

Piedmont Natural Gas - SVP, CFO

Michael Yount

Piedmont Natural Gas - SVP of Utility Operations

Frank Yoho

Piedmont Natural Gas - SVP - Commercial Operations

CONFERENCE CALL PARTICIPANTS

Jim Lykins

Hilliard Lyons - Analyst

PRESENTATION

Operator

Welcome to the Piedmont Natural Gas third quarter earnings conference. (OPERATOR INSTRUCTIONS). And as a reminder, this conference is being recorded.

I'll now turn the conference over to John Sutphin, Manager of Finance and Investor Relations. Please go ahead, sir.

John Sutphin - *Piedmont Natural Gas - Manager of Finance and IR*

Thank you, Kathy. Good afternoon. Thank you for joining our third quarter 2008 earnings conference call. This call is open to the general public and is being webcast live over the Internet. If you would like to access the webcast of this call, please visit our website at piedmontng.com and choose the investor's link. On the right-hand side of the page you will find a link to the webcast.

On the call today presenting prepared remarks we have Tom Skains, President, Chairman and Chief Executive Officer, and Dave Dzuricky, Senior Vice President and Chief Financial Officer. Other members of our executive management team are also in attendance. At the conclusion of the prepared remarks, we will open the discussion to questions. Finally, this call may include forward-looking statements within the meaning of the securities laws. Actual results may materially differ from those discussed in the forward-looking statements. More information about the risks and uncertainties relating to these forward-looking statements may be found in Piedmont's latest Form 10-Q which is available on the SEC's website at sec.gov. With that, I will turn the call over to Tom.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

Thanks, John. Before we begin today, I would ask that we first take a brief moment of silence in remembrance of this day seven years ago. Thank you. Good afternoon, everybody and thank you for joining us for our third quarter 2008 conference call. As you already know, we filed our third quarter 10-Q and issued our earnings release on Monday. I know many of you are interested in the progress of our North Carolina rate case as well as any new developments on our Robeson LNG storage project, and I'll get to those in just a moment but let me first walk through our financial performance.

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Due to the seasonality of our business, we typically experience losses in the summer months which make up our third quarter. This quarter our net loss of \$7.7 million, was \$1.5 million or 16% improved from the third quarter of 2007. Losses per share were \$0.10, which were \$0.02 or 17% improved from the third quarter of 2007. Year-to-date, our net income of \$123.2 million has increased \$10.5 million or 9% compared to the same period in 2007, and our earnings per share of \$1.68 is 11% improved from \$1.52 last year. Dave will walk through the specifics of the income statement in just a moment, but I want to take a note of our exceptionally strong third quarter in that we had 3% growth in margin resulting from continued growth in our residential and commercial markets as well as wholesale marketing activities and increased power generation margins. At the same time, O&M expenses fell 6% from last year's quarter and are down 3% year-to-date compared to the same period in 2007 as a result of our process improvement and cost reduction initiatives.

Regarding our North Carolina rate case, on August the 25 we, the North Carolina public staff and other interveners with the exception of the Attorney General's office, filed a settlement with the North Carolina Utilities Commission stipulating to an annual margin increase of 15.7 million along with the permanent extension of our margin decoupling mechanism. A hearing took place on Tuesday and we anticipate a decision from the North Carolina Utilities Commission in October so that new rates can be effective for the start of our fiscal 2009 year on November 1, 2008.

On last quarter's call we announced our intention to construct, own and operate a new LNG storage facility in Robeson County, North Carolina. I'm pleased to report that we have made substantial progress on that front, including securing purchase agreements for the land, rezoning the site for use as an LNG storage facility, and engaging Chicago Bridge and Iron as design contractor for the project. We have been enthusiastically received by local officials in the county and we continue our project development work. It is obviously still very early in the process, but we are optimistic that we can complete this project on time and within our previously stated capital expenditure range of \$300 to \$350 million.

Finally, you can see in our earnings release that we reaffirmed our guidance of \$1.45 to \$1.55 per share, but we're now emphasizing the upper range of that guidance in light of our strong year-to-date performance. We anticipate issuing our earnings guidance and capital budget for fiscal year 2009 which begins November 1 in late October. With that, let me turn the call over to Dave for a more detailed discussion of our third quarter financial results. Dave.

Dave Dzuricky - *Piedmont Natural Gas - SVP, CFO*

Thank you, Tom, and good afternoon, everybody. As you know, earnings per share was a loss of \$0.10 for the quarter compared to a loss of \$0.12 in last year's third quarter, as Tom had mentioned earlier. Specifically, margin for the quarter was up nearly \$2 million due to continued growth in our markets. And while we have seen our growth slow somewhat, we're still having year-on-year improvement in our top line. Income from our equity investments declined by \$1.6 million compared to last year, primarily due to higher operating costs of Hardy Storage. As you will recall, Hardy was in a startup mode last year and with underground storage there are typically startup expenses that end up being incurred early in the first few cycles of that storage operation.

We also had a slight unfavorable variance at SouthStar due to warmer weather this year compared to last year. Our O&M expense in the third quarter declined by \$3.1 million compared to last year. If you will recall, we had accrued severance benefits in last year's second quarter that were not incurred this year, and we continue to see the benefits of our process improvement initiatives. Our interest expense was down 8% this quarter compared to last year's quarter, primarily due to greater AFUDC accruals this year. All other expense categories tracked along their normal trends.

Relative to capital expenditures in the third quarter of 2008 our utility capital expenditures totaled \$58.2 million or \$25.3 million more than in last year's third quarter. As I mentioned during our last call, we had many infrastructure improvement projects this year compared to last, and the third quarter is a peak construction period for these types of investments and that's why we've experienced the uptick. So far the investments we have made in the Robeson project have been minimal. With that, I will turn the call over to John.

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John Sutphin - *Piedmont Natural Gas - Manager of Finance and IR*

Thank you, Dave. This concludes are prepared remarks and we now welcome your questions.

QUESTIONS AND ANSWERS

Operator

Thank you. (OPERATOR INSTRUCTIONS) Our first question comes from Jim Lykins with Hilliard Lyons. Go ahead, please.

Jim Lykins - *Hilliard Lyons - Analyst*

Good afternoon, gentlemen.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

Hi, Jim.

Jim Lykins - *Hilliard Lyons - Analyst*

You guys have made quite a bit of improvement with O&M. I'm just wondering if you could give us an idea on what's left with the business process improvements and maybe you could comment a little bit on how O&M as a percentage of margin will play out over the next year or so.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

Okay. Thank you, Jim. I'm going to let Dave answer that question in combination with Michael Yount, our Senior Vice President of Utility Operations. Dave.

Dave Dzuricky - *Piedmont Natural Gas - SVP, CFO*

Thank you, Tom and good afternoon, Jim.

Jim Lykins - *Hilliard Lyons - Analyst*

Hi, Dave.

Dave Dzuricky - *Piedmont Natural Gas - SVP, CFO*

We've had a lot of activity over the last couple of years and just to kind of go through the litany of what's taken place at Piedmont during that time in terms of our O&M, we've had a management restructuring. We've installed automated meter reading at all of our roughly 1 million customers' locations, we have had a consolidation of our business offices. We have had a consolidation of some of our call centers. We've redesigned the pension program for the company and we've also initiated a health and wellness program that has paid dividends, in our opinion, in terms of holding the line on medical costs and insurance premiums.

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Obviously, that is a lot of things that have been done to reconfigure the cost structures as it relates to O&M. But we continue to move forward in other areas of the company.

Let me just say, Jim, that we're not going to try to give you an idea of the trend of that for the next couple years, as Tom mentioned in his remarks, we'll be issuing our guidance in late October for 2009 and within that guidance will be all of our assumptions regarding how our O&M expense will behave next year. With that, let me turn it over to Michael to give you some background about what it is we're looking at as we move into 2009 and beyond.

Michael Yount - *Piedmont Natural Gas - SVP of Utility Operations*

Thanks, Dave. Hey, Jim.

Jim Lykins - *Hilliard Lyons - Analyst*

Hi.

Michael Yount - *Piedmont Natural Gas - SVP of Utility Operations*

In the operations area specifically, we're kind of focused on two areas of work. One is the service work that we do for our customers and the other is the construction and compliance work that we do. We've got ongoing projects in both of those areas that will help us in the way that we schedule, manage and measure that work and we expect those projects will continue to make us more efficient in the O&M area in operations, especially during the next two years. As Dave said, with regard to specifics, any improvements we make along the way will build into our guidance in the time period in question.

Jim Lykins - *Hilliard Lyons - Analyst*

Well, let me ask it this way. And I understand that you're hesitant to talk about specific numbers, but given what you're saying about, say, construction and compliance, would at least be fair to assume that those margins will improve in '09 relative to '08?

Dave Dzuricky - *Piedmont Natural Gas - SVP, CFO*

No, I don't think it's fair to assume anything. I think what's fair to assume, Jim, and I'm really not trying to be disingenuous with you, is what's fair to assume is that when we give you the guidance, all of our thinking around those issues will be included in that.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay.

Dave Dzuricky - *Piedmont Natural Gas - SVP, CFO*

And that's kind of where we are right now.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay.

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Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

I would also refer you to the 10-Q on some of the margin development that will impact '09 from our regulatory activities in North Carolina and South Carolina. Those regulatory proceedings are pending actions by the utilities commission but it may give you a flavor of the work we've been doing and the regulatory arena. That will impact margin and margin growth in addition to the organic growth that we continue to see in the regional markets that we serve, adding new customers to the system.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay. That's helpful. And could you also talk about what you're seeing right now with customer growth and maybe what the new construction market is like in Charlotte right now.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

Sure. I'm going to ask Frank Yoho to talk about that generally, not just related solely to Charlotte but what we see across the system.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay.

Frank Yoho - *Piedmont Natural Gas - SVP - Commercial Operations*

Okay, Jim, how are you doing today?

Jim Lykins - *Hilliard Lyons - Analyst*

Good, how are you?

Frank Yoho - *Piedmont Natural Gas - SVP - Commercial Operations*

Good, thank you. As we mentioned before, we have seen a slowing of new construction specifically in the residential market sector but we're probably fortunate relative to the rest of the country. The range we've moved is from a 2% to 2.5% range right now and we're watching it closely as we move forward. Right now that's where we're sitting. Off of where we have been relative to much of the country we're in better shape.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay. And --

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

This is Tom Skains. I would add that we do see some improvements, frankly, year to year in our conversion market that we talked about in past discussions and most of the decline occurring here obviously in the residential new construction arena. So we work hard to market the value of our product across the markets that we serve, continuing growth in the residential new construction market, albeit slower than it has been in years past. But with a renewed emphasis on the conversion market, and

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that is convincing customers when their appliances are ready to be replaced, to choose natural gas as opposed to other energy sources.

Frank Yoho - *Piedmont Natural Gas - SVP - Commercial Operations*

We've been also very successful in maintaining the attractiveness of natural gas on a relative basis to other options, while we've seen the overall market decline some, the acceptance of the natural gas has not declined, as Tom mentioned, especially the east. There's still a number of propane opportunities, we tend to target those existing residences for conversion.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay. And lastly, could you tell us if there are -- or is there anything you can tell us regarding the time line of your storage project in addition to the update that you gave in your prepared remarks?

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

Yes, I'll ask --

Jim Lykins - *Hilliard Lyons - Analyst*

just what we can look for going forward.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

I'll ask Michael to address that generally. You will see first, though, in our guidance for 2009 that we hope to issue in late October also our capital budget for 2009 and embedded in that will be capital for our traditional utility operations, but also capital for the LNG growth project. So it will be embedded in that guidance.

Jim Lykins - *Hilliard Lyons - Analyst*

Okay.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

We still feel good about the overall estimate that we gave you and, Michael, why don't you summarize the period of time we think this project will be under construction and hopefully placed into service.

Michael Yount - *Piedmont Natural Gas - SVP of Utility Operations*

Yes, happy to, Tom. Jim, we're actually a little bit ahead of schedule. We're in the middle of negotiating our construction contract and that will allow us to sort of lock things in by January of '09 and after that we should be able to begin construction. So all the way around, the project is just going extremely well and we're happy that we're actually a little bit ahead of schedule. But construction should start some time in '09, probably in the spring.

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Jim Lykins - *Hilliard Lyons - Analyst*

Okay. Good to hear. All right. Thank you, gentlemen.

Tom Skains - *Piedmont Natural Gas - Chairman, President, CEO*

Thanks, Jim.

Operator

Thank you. (OPERATOR INSTRUCTIONS). We have no further questions.

John Sutphin - *Piedmont Natural Gas - Manager of Finance and IR*

Thank you, Kathy. As always, we thank you for your interest in Piedmont Natural Gas and for taking time to be with us today. If you have any further questions pertaining to our third quarter results, please contact our Investor Relations department. This concludes our third quarter 2008 earnings call.

Operator

Thank you. Ladies and gentlemen, that does conclude our conference for today. Thank you for your participation and for using AT&T executive teleconference. You may now disconnect.

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