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PNY - Q2 2010 Piedmont Natural Gas Earnings Conference Call

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CORPORATE PARTICIPANTS

Robert Pritchard

Piedmont Natural Gas - Vice President, Treasurer, Chief Risk Officer

Tom Skains

Piedmont Natural Gas - President, Chairman, CEO

Dave Dzuricky

Piedmont Natural Gas - SVP and CFO

Kevin O'Hara

Piedmont Natural Gas - SVP of Corporate & Community Affairs

CONFERENCE CALL PARTICIPANTS

Dan Fidell

Brean Murray, Carret & Co. - Analyst

PRESENTATION

Operator

Good day, everyone and welcome to the Piedmont Natural Gas Second Quarter Earnings Conference Call. Today's conference is being recorded.

At this time, I'd like to turn the conference over to Mr. Robert Pritchard, Vice President, Treasurer, and Chief Risk Officer. Please go ahead, sir.

Robert Pritchard - *Piedmont Natural Gas - Vice President, Treasurer, Chief Risk Officer*

Thank you, Robbie.

Good morning everyone and thank you for joining the Piedmont Natural Gas Second Quarter 2010 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 piedmontnaturalgas.com and choose the investor's link. On the right hand side of the page, you'll find a link to the webcast.

On the call today, presenting prepared remarks, we have Tom Skains, President, Chairman, Chief Executive Officer, Dave Dzuricky, Senior Vice President, Chief Financial Officer. Other officers of the Company are also in attendance. At the conclusion of the prepared remarks we will also open the call to your questions.

Finally, this call may include forward-looking statements and our actual results may materially differ from those statements. More information about the risks and uncertainties related to these forward-looking statements may be found at Piedmont's latest Form 10-K.

With that I'll turn the call over to Tom.

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

Thank you, Rob and good morning everybody and thank you for joining us for our second quarter 2010 earnings conference call. We saw many of you at the AGA Financial Forum just a few weeks ago, and I appreciate you taking the time to join us again



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today. As you know, we filed our second quarter 10-Q this morning and issued our second quarter earnings release late yesterday. I'm going to provide you the highlights for the quarter and then turn the call over to Dave for a more detailed discussion of our financial results.

Let's start on slide two, since Rob has already covered the forward-looking statements advisory on slide one. This quarter we earned net income of \$46.8 million, or \$0.65 per share. We added 2,362 new customers during the quarter and 5,428 new customers for the year-to-date, for an annualized growth rate of about 1.1%. As you know, we also announced during the quarter a project to provide natural gas service to Progress Energy's proposed Sutton Power Generation Plant in eastern North Carolina. Also in our release we reaffirmed our fiscal year 2010 earnings guidance of \$1.90 to \$2 per share, including the gain on the sale of our half interest in SouthStar energy that we recognized in the first quarter.

On slide three you can see that our second quarter net income decreased about 13% compared to the second quarter of 2009. This was in large part due to the decreased contributions from SouthStar as a result of our lower 15% ownership interest. In addition, net income declined as a result of gas cost adjustments to margin, increased O&M due to higher payroll and pension expenses, and higher interest expense. I'll let Dave speak to details of our income statement in just a moment.

On slide four we've highlighted our gross customer additions for the quarter and for the year-to-date. As you can see, the year-to-date comparison shows slower customer growth due to pressure in the residential and commercial new construction markets. However, we're encouraged that our residential new construction additions were higher this quarter than they were a year ago. We are cautiously optimistic that this is a sign of stabilization in a new housing market. In addition, our sales force continues to focus on the conversion market, and our customer additions there exceeded last year's totals for both the quarter and for the year-to-date. Everything considered, we still see forecasted gross customer addition growth of about 1% to 1.2% for 2010.

As we discussed at the AGA Financial Forum, another source of growth for our Company is in the power generation market. We've executed five contracts, two with Duke and three with Progress Energy, to provide natural gas service to new combined cycle power generation plants in North Carolina during the 2011 to 2013 time frame. We will be investing about \$360 million in transmission pipelines and compression to provide long-term natural gas transportation service to these plants.

On slide five, we've updated our capital expenditure forecast for fiscal years 2010 through 2013. We now anticipate spending about \$224 million in utility CapEx in fiscal year 2010, compared to our latest estimate of about \$212 million. You'll also notice that the CapEx figures for 2011 through 2013 have been updated since our presentation at the AGA Financial Forum. While the total CapEx for power generation remains the same, we anticipate that more spending will occur in 2011 than was originally forecasted. Due to the size and nature of these projects, it's not uncommon to see capital spending revisions as these projects move through the project development phases to completion.

Finally, before I turn the call over to Dave, let me briefly update you on our regulatory strategy in Tennessee as I promised on last quarter's call. During this quarter, we examined our business in Tennessee, including our forecasted cost and revenues, and have decided not to pursue a rate case there this year. As we do each year, we will again evaluate the need for rate cases in all our jurisdictions in 2011.

And with that, I'd now like to turn the call over to our Senior Vice President and CFO, Dave Dzuricky.

Dave Dzuricky - Piedmont Natural Gas - SVP and CFO

Thank you, Tom, and good day to everyone.

As Tom indicated, our second quarter net income was \$46.8 million, or \$0.65 per share. Let me walk you through the major line items of our second quarter income statement, and then I'll turn the call back over to Rob to take your questions. Picking back



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up on slide six, margin of \$169 million was 1% lower than in the second quarter of 2009. The decline was due to period to period net gas cost adjustments, which offset our increased margin from industrial customers. We had positive adjustments in the second quarter of 2009 that gave some uplift to that quarter. We remain encouraged with the rebound in industrial volumes and view this as a leading indicator of economic recovery in our service territory.

On the expense side, operation and maintenance expense of \$58 million increased 8% from last year. This was due to higher payroll and pension expense. Regarding future expenses, during the quarter we started analyzing how the recently signed healthcare legislation will affect our run rate on O&M. Based on our analysis, and we did have a third party assisting us in that, we do not at this time believe legislation will have any material effect on employee expenses going forward.

On slide eight, income from joint ventures was \$13 million this quarter, 25% lower than in the second quarter of 2009. While earnings at SouthStar were basically flat, this is the first quarter we've operated with a 15% earnings and ownership interest, compared to a 30% ownership and 25% earnings interest in prior periods, so hence the decline.

On slide nine, we've shown our utility interest charges for the quarter at \$13 million, 9% higher than last year. Interest on long-term debt was lower due to lower amounts outstanding, and interest on short-term debt was lower because of lower borrowings and a lower average rate. However, these two decreases were more than offset by lower net interest income due to lower amounts due from customers to the Company. All other income statement categories tracked along their normal trends.

Finally, on slide ten, we've shown a historical trend of our annual earnings per share breaking out the earnings related to our utility and non-utility businesses. Not only have we grown overall earnings per share, but we've also been able to grow our core utility earnings. Looking to the future, the utility returns we'll gain from the five new power generation projects Tom mentioned will help us continue to grow our utility business. Given the reaffirmation of our 2010 guidance of \$1.90 to \$2.00 per share, including the gain from the SouthStar sale, we anticipate another excellent year at Piedmont.

With that, Rob, I'll turn it back to you.

Robert Pritchard - *Piedmont Natural Gas - Vice President, Treasurer, Chief Risk Officer*

Thank you, Dave. Robert, we are now ready to open the call for questions.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions).

We'll go first to Dan Fidell with Brean Murray, Carrett.

Dan Fidell - *Brean Murray, Carret & Co. - Analyst*

Good morning and thanks for the call.

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

Good morning, Dan.



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Dan Fidell - *Brean Murray, Carret & Co. - Analyst*

Just a couple of follow-up questions.

The first question is can you give us kind of an update on where contract negotiations stand with your union employees? It's my understanding that that comes up in June. Is that correct?

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

Yes, it does, and those negotiations are under way; and I'm going to ask Kevin O'Hara to give you a brief update on that.

Kevin O'Hara - *Piedmont Natural Gas - SVP of Corporate & Community Affairs*

The existing contract expires June 27, and we continue negotiations. We're optimistic to have those negotiations completed by the end of June, with agreement around new contract terms.

Dan Fidell - *Brean Murray, Carret & Co. - Analyst*

Okay. Is there any more specifics you can give us in terms of what's included in those negotiations or is that still just private, part of the ongoing negotiations?

Kevin O'Hara - *Piedmont Natural Gas - SVP of Corporate & Community Affairs*

It is. I really can't go into any detail around any of the specific terms.

Dan Fidell - *Brean Murray, Carret & Co. - Analyst*

Okay.

Just a second question on Sutton and Wayne County. Engineering and specs I'm assuming for the next six months is where you guys are going to be spending most of your time with a big piece of the build beginning in 2011. Is all of that going on track and on schedule?

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

Yes Dan, everything is going according to schedule at this point. When we spoke at the AGA financial forum, of those five contracts that we mentioned, four had already been approved by the North Carolina Utilities Commission. The fifth one was approved just earlier this week.

So we have all of the contract approvals now we need from the North Carolina Utilities Commission and now we're set out to do more definitive engineering work, go about the process of permitting, right of way acquisition, leading eventually to construction of the projects to meet the scheduled in service dates. From a regulatory standpoint, we are through the heavy lifting. The contracts are all completed. They've been approved by the regulatory authorities and now we're just proceeding with the heavy lifting operations, engineering, permitting and construction work.



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Dan Fidell - *Brean Murray, Carret & Co. - Analyst*

Great.

Just a final, quick question on customer growth. You mentioned, I think, in the last few calls an improvement, especially on the industrial side. Is it reasonable for us to assume as we look forward into 2011 and 2012 that you're encouraged by what you've seen, that we can reasonably notch up our customer growth assumptions maybe even just a little bit for those out years?

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

Well, on the industrial side, we're mostly looking at volumes there; and remember last year in January at really the deepest part of the economic recession, we saw Frank about a 10% decline in Industrial volumes. We've now recovered more than half of that and as Dave mentioned, we feel good that we're seeing signs of economic recovery in the industrial market.

In the new construction conversion market, we've given you some information in the slide deck today which shows that although we're down year-to-date this year compared to last year on total customer additions, if you look at quarter to quarter comparisons, things are starting to stabilize there as well. Our conversion additions are higher than they were a year ago. The commercial new construction market is down slightly, but it always lags the residential market somewhat and in the residential new construction market, actually, we've seen slightly higher additions in the second quarter of this year than we did last year.

Again, we're cautiously optimistic that things are stabilizing somewhat, but I think it's premature to say at this point what that will foretell in terms of future growth in our customer additions in the out years. Again, for this year, we're forecasting somewhere between 1% to 1.2%. We feel we're on target for that. We'll be giving you more guidance later in the year for the next fiscal year, probably in the October, November time frame.

Dan Fidell - *Brean Murray, Carret & Co. - Analyst*

Great. Thanks for your comments, Tom.

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

Thank you.

Operator

Thank you. (Operator Instructions).

At this time, it appears there are no further questions in queue. I'd like to turn it back over to the presenters for any additional or closing comments.

Robert Pritchard - *Piedmont Natural Gas - Vice President, Treasurer, Chief Risk Officer*

Thank you, Robbie. This concludes our second quarter 2010 earnings conference call. Thank you all for joining us this morning. Thank you.

Operator

That does conclude today's call. Thank you for your participation.

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