
MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you very much for standing by. We appreciate your patience today and good afternoon. Welcome to the Piedmont Natural Gas Company's first quarter 2005 earnings conference call. [Operator Instructions]. As a reminder, today's call is being recorded for replay purposes and we ask that you stay online at the conclusion of the call to receive that replay information.

Well with that being said, let's get right to this first quarter's agenda. And here with our opening remarks is Piedmont Natural Gas Company's Director of Investor Relations, Mr. Headen Thomas. Please go ahead, sir.

Headen B. Thomas, Director of Investor Relations

Thank you and good afternoon, and thanks for joining us for our first quarter earnings conference call. Our earnings release was issued this past Friday, March the 4th. If you do not have a copy of the release, it is available on our web site at piedmontng.com. With me today for the conference call are Tom Skains, our Chairman, President and CEO; Dave Dzuricky, our Senior Vice President and CFO; Frank Yoho, our Senior Vice President of Commercial Operations; Kevin O'Hara, our Vice President of Business Development and Ventures, and other members of our management team.

Before the discussions begin, I would like to advise you that our comments address Piedmont's business outlook and contain certain forward-looking statements. These forward-looking statements are subject to a number of risks and uncertainties and actual results may differ materially. Please refer to pages 26 and 27 of our 2004 Annual Report to Shareholders and our most recent SEC filings for information about the risk factors that could cause actual results to differ.

Now, I'll turn the call over to our Chairman, President, and CEO, Tom Skains.

Thomas E. Skains, Chairman, President, and Chief Executive Officer

Thank you, Headen. Welcome everyone, and thanks for participating in our first quarter 2005 earnings conference call. I'd like to thank those of you who were in Nashville last Friday for Annual Shareholders Meeting. It was good to see many of you there. As you probably noticed, in addition to the earnings release this past Friday we also announced our 27th consecutive annual dividend increase. The dividend was increased 7% from 21.5 cents to 23 cents per share. The dividend has increased, by the way, an average of 6.6% over that 27-year period.

With the first quarter behind us, I'd like to take just a second and update you on some of our priorities for fiscal year 2005. I outlined these as well last Friday at the Shareholders Meeting. First, we will continue to advocate the need for national energy legislation that would balance natural gas supply and demand. We support an energy policy that encourages the development of new domestic natural gas supplies and delivery infrastructure to meet increasing customer demand for our product at reasonable competitive prices.

We initiated our CBPI [Continuous Business Process Improvement] program in 2004 in order to implement best practices, achieve cost efficiencies, and improve customer service. Some of the key initiatives we will be working on to implement this year and over the next two to three years include consolidating our customer call centers and regional business offices, automated meter

reading functions, and consolidating some of our smaller local business offices into nearby larger district offices. These activities are proceeding according to plan and their financial impact has already been included in our fiscal year 2005 earnings guidance.

Switching to subject of rate relief, last Monday on February 28, we filed a letter of intent to file a general rate case proceeding in North Carolina this year. As a part of that case, we will propose to consolidate all of our North Carolina operations under one tariff, one set of service regulations, and one rate structure. We expect to file the North Carolina case by March 31, with new rates effective November 1, the beginning of our 2006 fiscal year.

Separately, on February 16, the Governor of South Carolina signed the Natural Gas Rate Stabilization Act into law. This legislation allows gas utilities in South Carolina, upon election, to file for annual rate adjustments to ensure that the utility's earnings stay within a 50 basis point band of its allowed return on equity. Our current allowed return on – rate of return on equity is 12.6% in South Carolina. The Act provides for a less costly and more efficient regulatory process, and increased flexibility for utilities to expand their distribution systems to provide service to new customers. We expect to rely on this new law and file for rate adjustment this year and reset rates in South Carolina effective November 1, 2005, the beginning of our 2006 fiscal year.

Now on today's conference call, Frank Yoho will address our commercial operations. Dave Dzuricky will conduct our financial review, and Kevin O'Hara will cover our joint venture activities. At the conclusion of our prepared remarks, we will open up the session for a Q&A period. Now I'd like to turn the call over to Frank Yoho. Frank?

Franklin H. Yoho, Senior Vice President, Commercial Operations

Thank you, Tom. Starting with volumes. For the quarter, volumes were down slightly from last year due to weather that was warmer than normal and also warmer than last year's weather. For the quarter this year, we experienced weather which was 9.6% warmer versus last year's 3.8% warmer. And accordingly our volumes for this year were 71.7 Bcf compared to 73.5 Bcf for the quarter of last year.

Margins – because of our weather normalization adjustment and the continuing growth we experienced on our system, margins were up quarter-to-quarter. This year our margins were \$202.6 million versus last year's quarter margins of \$196.5 million. We're also seeing improvement in customer additions, with this year's first quarter results being 9,570 new customers added versus last year's 8,077 customers added. Because of a relatively mild and stable winter, our wholesale marketing shareholder margins were down slightly, this year being \$1.5 million compared to last year's \$2 million. And on the gas supply front, we continue to execute our hedging plans to protect our customers against significant price spikes.

On a storage perspective, as is the case from a national perspective, Piedmont storage facilities have not been drawn down as much this year as last year, along with not as much as historical averages. On the industrial marketing front and fuel switching, while margins are up slightly in this segment, we've still seen some market loss to Number 6 fuel oil, but we continue to be competitive and are successful in retaining the Number 2 market, which is most prevalent on our systems.

Back to you, Tom.

Thomas E. Skains, Chairman, President, and Chief Executive Officer

Okay, thank you, Frank. Now I'd like to turn the call over to Dave Dzuricky, who is going to review our financial results. Dave?

David J. Dzuricky, Senior Vice President and Chief Financial Officer

Thank you, Tom. Appreciate that, and good afternoon, everybody. We were pleased with the first quarter financial results for fiscal 2005 with earnings per share at 93 cents. As you will recall and was noted in our press release, one-time gains of \$4.6 million in the first quarter of 2004 skewed the comparison somewhat. Also, the first quarter of 2005 has the full effect of the 8.5 million shares we issued in January 2004 to partially finance the NCNG transaction. The difference in shares outstanding in the two quarters amounts to 11 cents a share dilution in the first quarter of fiscal 2005.

As you will note, O&M expense remains under control due to the effort of all of our employees. And for that we are very grateful.

I would also note that general taxes are up significantly in this quarter compared to last year. In the first quarter of 2004, as noted in our 10-Q from that period, we received a property tax refund of \$1.8 million due to a favorable court ruling. The first quarter of 2005 reflects a more "normal" level of general taxes.

We are tending to our knitting this year and the results reflect the good effort put forth by all of our employees in the first quarter. Tom, let me turn it back to you.

Thomas E. Skains, Chairman, President, and Chief Executive Officer

Okay, thank you, Dave. Now I am going to ask Kevin O'Hara to give us a joint venture overview. Kevin?

Kevin M. O'Hara, Vice President, Business Development and Ventures

Thank you, Tom. And I am going to cover our first quarter earnings in '05 from our joint ventures in Cardinal, Pine Needle, SouthStar, and I will also provide a brief update on Hardy Storage project. And the earnings that I will cover are Piedmont's share of the earnings from these joint ventures.

Cardinal, this is our North Carolina intrastate pipeline joint venture of which Piedmont has a 21.5% ownership interest. In the first quarter of '05, earnings were \$304,000 versus \$283,000 in the first quarter of last year, '04. Primarily the reason for that is a higher level of O&M expenses.

Pine Needle LNG, this is our FERC-regulated 4 Bcf interstate storage facility in Guilford County, North Carolina. Piedmont has a 40% ownership interest in Pine Needle. In the first quarter of '05 our earnings were \$644,000 versus \$587,000 dollars in the first quarter of last year. And similar to Cardinal, '04 had a higher level of O&M expenses in the first quarter.

SouthStar, this is our retail marketing joint venture with AGL Resources, of which Piedmont has a 30% ownership interest. Our earnings share, though, is 25% for SouthStar. In the first quarter of '05, earnings were \$2.7 million versus \$3.3 million for the first quarter in '04, and that variance is primarily due to a \$1.5 million one-time earnings pick-up we had in the first quarter of '04 that resulted from our restructuring of the disproportionate sharing provisions.

For Hardy, this is our new joint venture with Columbia Gas Transmission to design and build and operate a 12.4 million dekatherms natural gas storage facility in Hardy County, West Virginia. Piedmont is also a customer of Hardy, it is fully subscribed under long-term contracts and we are still expecting Hardy to go into service beginning in April 2007. We are planning to file for a

certificate with FERC the first week of April with the expectation that we'll receive a certificate in September, October timeframe.

Tom, back to you.

Thomas E. Skains, Chairman, President, and Chief Executive Officer

Okay, thank you, Kevin. And now I'd like to turn the conference call back over to Headen Thomas, who is going to conduct our Q&A session. Headen?

Headen B. Thomas, Director of Investor Relations

Thank you, Tom. Brad, I believe that we are ready for you to kick off the Q&A session.

QUESTION AND ANSWER SECTION

Operator: Indeed, I'd be happy to, and thank you very much, everyone. [Operator Instructions]. And representing Janney Montgomery we'll go to the line of David Schanzer. Please go ahead, sir.

<Q – David Schanzer>: Hi, good afternoon.

<A – Thomas Skains >: Hi, David.

<Q – David Schanzer>: Couple of questions. First of all, it seems that a lot of what happened in the first quarter had to do with O&M, both SouthStar and the company in general. For purposes of our modeling going forward, can we assume that there will be some higher O&M quarter-to-quarter comparisons, but maybe not a whole lot higher than we saw in the first quarter? More like the rate of inflation kind of thing?

<A – David Dzuricky>: David, this is Dave Dzuricky. I would say that's correct. We did do a great job of blocking and tackling in the first quarter compared to last year. As you know, and everybody on the call knows, medical cost increases are still running near double-digit levels, and so to continue to hold O&M growth at approximately 1% year-on-year is going to be difficult. But we are going to give it our best.

<Q – David Schanzer>: Okay. And then as far as the economy, in terms of adding new customers, was the experience in the first quarter in line with what you were expecting in terms of the number of new customers added? And do you think you will hit your target for the year?

<A – Thomas Skains>: Actually, David, this is Tom Skains. It was a little more robust than we were planning for. And Frank Yoho can share some of this good news with you.

<A – Franklin Yoho>: Yeah, we were very pleased with the results. And what we can continue to see in residential new construction, driven by the economy in this area and also by low mortgage rates, very strong numbers in that area. But also on top of that, which is a little bit more representative of a strengthening economy, is our commercial additions were up 14% compared to last year. So all of the numbers that are coming in should continue to have a pleasant year in that area.

<Q – David Schanzer>: The commercial additions, were they the small C&I or the large C&I?

<A – Franklin Yoho>: Smaller C&I that tends to follow residential construction.

<Q – David Schanzer>: Wow, okay. And then lastly, if could you comment a little bit about what is going on in Eastern North Carolina, what kind of progress has been made?

<A – Thomas Skains>: Okay, David. I am going to ask Kevin to give you a report on that. He is actually on the board at EasternNC and is our liaison with that joint venture.

<A – Kevin O'Hara>: Thanks, Tom. We continue to make progress in Eastern North Carolina in terms of spending the bond funds that were approved for that project. There were \$188 million of bond funds approved. We have invested or spent about \$170 million of those bond funds.

Operator: And I beg your pardon, sir. Your line just cut out.

<A – Kevin O'Hara>: I'm sorry – and in terms of completing the project, we are currently looking at the end of this summer for that project to be built out based on the scope that was approved by the North Carolina Utility Commission.

<Q – David Schanzer>: Okay. And when do you think we will start to it see significantly impact results?

<A – Thomas Skains>: David, there will be some additional information on EasternNC in our Q, which will be filed late this week. Is that not correct, Barry? [Barry L. Guy, Vice President and Controller]

<Q – David Schanzer>: Well, we certainly can wait. Thank you.

<A – Thomas Skains>: Yeah, I would wait – wait and read some of the statements in the Q. It may give you some information in that respect.

<Q – David Schanzer>: Great, thanks a lot.

Operator: And thank you, Mr. Schanzer. And next, representing Zimmer Lucas Partners, we go to the line of Reza Hatefi. Please go ahead.

<Q – Reza Hatefi>: Good afternoon. Thanks for taking my question. Can you give us an update on CapEx going forward, maybe '05, '06?

<A – David Dzuricky>: Yeah, Reza, this is Dave Dzuricky. Thanks for the question. First of all, let me answer the easy part. We're not going to give out a forecast of capital expenditures for fiscal 2006. For fiscal 2005, as Frank mentioned, we're running ahead on our customer growth, although we have made adjustments in other areas in order to keep ourselves within the approved budget of \$163.7 million. So we will exercise discipline around our capital budget in order to accommodate the more vibrant growth that we're experiencing. Hopefully that will continue through the rest of the year. But at this point in time, and underlying the reiteration of our guidance for the year is that capital budget that was previously announced at \$164 million.

<Q – Reza Hatefi>: And, sorry if I missed this, but is there a charitable contribution in guidance? And if so, is it the same amount as last year?

<A – David Dzuricky>: The contribution of \$7 million that we made to the Piedmont Natural Gas Foundation in fiscal 2004 really reflected the effect of the one-time gains that were realized in the first quarter from our non-utility operations. Piedmont, as matter of course, continues to contribute and invest in its communities throughout the year. We would expect a normal program this year, with some enhancement due to the existence of the Foundation.

<Q – Reza Hatefi>: But not like a – but we shouldn't expect a large one, like last year, of course?

<A – David Dzuricky>: That's correct, Reza.

<Q – Reza Hatefi>: Okay. And for your upcoming North Carolina rate case filing, what test year are you going to file under?

<A – David Dzuricky>: It's going to be the calendar year 2004.

<Q – Reza Hatefi>: Okay. Thank you very much.

<A – David Dzuricky>: Yes, sir.

Operator: [Operator Instructions]. And next in queue is Michael Creager with BB&T Capital Markets. Please go ahead.

<Q – Michael Creager>: Good afternoon.

<A>: Hi, Michael.

<Q – Michael Creager>: Hi. Related to that last CapEx question, can you maybe breakout some of the major components of that \$164 million. It's a bit up this year versus last year.

<A – David Dzuricky>: Yes, it is. Of course you've got – in there you have got a baseline for what we normally invest in order to maintain the safety and reliability of the system, what we would call – I would call, anyway, a nondiscretionary kind of investment in order to maintain the system as well as to increase deliverability because of our growth out in the fingers of our system. Secondly, you have what I would call efficiency investments, and those are up this year because of the continuous business process improvement project. We will be investing in a number of areas in order to reduce O&M expense in future years. And then finally, you have the revenue-producing growth, which is the bulk of our investments in capital expenditures. The blip we are probably seeing – or the blip you are seeing, Michael, probably relates to those efficiency investments. Those in the budget are up quite a bit from what they have been in the past.

<Q – Michael Creager>: Okay. So a base number is somewhere around 140 or so?

<A – David Dzuricky>: That's probably – that would be in the ballpark.

<Q – Michael Creager>: Okay. And then on the – could you guys tell me what you're assuming for a regulatory return in North Carolina that's sort of baked in your '05 guidance?

<A – David Dzuricky>: We really don't bake in an allowed rate of return or an earned rate of return in each state, Michael. What we do is we set our guidance around our expectations based on coming out of our budgeting process, as well as with collaborative deliberations, both with our Board, generally, as well as with our Audit Committee in particular. But what we look at is the margin delivering capability of the company – in fiscal '05, it happens to be without a rate case – as well as our ability to contain the growth in other areas of expense, most notably operation and maintenance expense. We also look to our non-utility operations and the environment in which they are operating to determine what kind of overall income could come from that quarter.

<Q – Michael Creager>: Okay. So the rate request, there is going to be some rate relief in that. It's not just to sort of consolidate legacy Piedmont and NCNG, right?

<A – Thomas Skains>: Yes, there will be both. There will be rate relief, as well as the consolidation proposal, and we are still sorting through all of the test period data and putting together our strategy in the case. And we haven't sorted out yet what overall return or return on equity we'll be filing yet. But what we will be filing will not be effective until November of this year and won't impact '05 fiscal year earnings, but will impact '06 earnings instead.

<Q – Michael Creager>: Thank you very much.

Operator: And thank you, Mr. Creager. With that, Mr. Skains, Mr. Dzuricky, and our host panel, I'll turn the call back to you. There are no further questions.

Headen B. Thomas, Director of Investor Relations

All right. Thank you. At this time, I would like to turn the call back over to Tom Skains for closing remarks.

Thomas E. Skains, Chairman, President, and Chief Executive Officer

Okay, thank you, Headen. Let me just reiterate what Dave said earlier. We are pleased with our first quarter results. We think we are off to a very solid start in 2005. And, as always, we thank you for your interest in and support of our company. And we look forward, as well, to seeing many of you at the AGA Financial Forum in May. So, until then, have a great spring.

Operator: And ladies and gentlemen, your host is making today's conference available for digitized replay. It's for two weeks, starting at 6 p.m. Eastern Standard Time March the 7th all the way through 11:59 p.m. March the 21st. To access AT&T's Executive Replay Service, please dial 800-475-6701, and at the voice prompt enter today's conference ID of 771034. And that does conclude our earnings conference for this quarter. Thank you very much for your participation, as well as for using AT&T's Executive Teleconference Service. You may now disconnect.

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