
MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. And welcome to the Second Quarter Teleconference. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session with instructions given at that time. [Operator Instructions]. As a reminder, this teleconference is being recorded. I would now like to turn your teleconference over to the Senior Vice President and General Counsel, Mr. Kim Cocklin. Please go ahead sir.

Kim R. Cocklin, Senior Vice President, General Counsel and Chief Compliance Officer

Thank you Bill very much. Good afternoon and thank you for joining the second quarter earnings conference call for Piedmont Natural Gas. The company's earnings were publicly released on Tuesday, June 7th and our 10-Q was filed on Thursday, June 9. Both releases are available for your review and inspection on our website at piedmontng.com.

In attendance today for the company include all members of the senior management team and the presenters include Tom Skains, our Chairman, CEO and President; Dave Dzuricky, Senior Vice President and Chief Financial Officer; Frank Yoho, our Senior Vice President of Commercial Operations and Kevin O'Hara, Vice President, Business Development and Ventures.

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. I would ask you to please refer to page 26 and 27 of our 2004 Annual Report to shareholders and our most recent SEC filings for information relating to the risk factors that could cause actual results to differ.

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

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

Thank you, Kim. Welcome everybody and thanks for participating in our second quarter earnings conference call. Before we update you on our second quarter results, I would like to review some of our priorities for fiscal year 2005. First, we continue to advocate the need for national energy legislation that would balance natural gas supply and demand. We are encouraged by the progress made thus far by the US House and Senate and are hopeful that we will see a positive energy bill later this year.

As you know, 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 are implementing over the next two to three years include consolidating customer call centers and regional business offices, automating meter reading functions, and consolidating some of our smaller local business offices into nearby larger district offices. All of these initiatives are well underway and are proceeding according to plan. Their financial impact has been included in our fiscal year 2005 earnings guidance.

Switching to the subject of rate relief, on April 1st, we filed a general rate case proceeding in North Carolina. In addition to seeking necessary cost increase recovery, we have proposed a consolidation of all of our North Carolina operations under one tariff, one set of service regulations and one rate structure.

Separately, the Natural Gas Rate Stabilization Act was approved on February 16th in South Carolina. The Act provides for a less costly and more efficient regulatory process. We plan to make an election under this new law and file for a rate adjustment by June the 15. We expect that new base rates in both North Carolina and South Carolina will become effective November 1st, 2005, the beginning of our 2006 fiscal year.

Finally, I would like to say that our business this year is proceeding according to plan and as you will note in our second quarter press release, we affirmed our fiscal year 2005 guidance of \$1.23 to \$1.30 per diluted share.

Next on today's conference call, Frank Yoho will address our commercial operations, followed by Dave Dzuricky, who will conduct our financial review and then Kevin O'Hara will cover our joint venture activities. After that, we will have a Q&A session at the conclusion of our prepared remarks.

So now, I would like to turn the call over to Frank Yoho.

Franklin H. Yoho, Senior Vice President, Commercial Operations

Thank you, Tom. Second quarter results in regards to volumes for '05 were 59.4 Bcf in '05 versus 57.8 Bcf in '04. The volume gains we have seen here were primarily in power generation. For our core markets we have actually seen a slight decline. Margins for the second quarter in '05 were \$140.7 million versus 145.8 million in fiscal '04 second quarter. This is down primarily due to reduced usage by our core markets caused by conservation we believe driven by high commodity costs of gas.

Customer growth additions have been strong. We have seen strong results in our commercial and new residential construction markets. This year to date – this year, year-to-date – we have seen 16,600 new connects versus approximately 14,800 new connects during fiscal year '04.

Our wholesale marketing group achieved results for the second quarter of 1.5 million versus results of 1.4 million in the second quarter of '04. We continue to implement our hedging plans for future gas supply purchases and our storages are in good shape for both the company and an industry, relative to last year and historical averages.

The industrial market is relatively stable with continued success in competing for the Number 2 load, which is our largest alternate fuel load on our system and we continue to be challenged with the price in the Number 6 fuel load market.

And now, I would like to turn it over to Dave Dzuricky to review our financial results.

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

Thank you, Frank. Good afternoon everybody. Not a whole lot to report on the financial side. Of course, you do have the 10-Q available to you should you have any questions. Let me just summarize by saying and reminding you that diluted earnings per share for the quarter were \$0.52 versus \$0.54 in the prior year's second quarter and we were pleased with that performance.

As you will note, in both our press release and in our 10-Q, our O&M expense was up 4% in the quarter-to-quarter comparison, but in the second quarter of fiscal '05, we did have an additional accrual related to our vacation of \$1.2 million. Absent that additional accrual, the year-to-year O&M expense would have risen about 1%.

We've also had a strong performance from our joint ventures that Kevin O'Hara will discuss in a bit. And as mentioned by Tom and as reported in our press release of June 7th, we've reaffirmed our guidance for the year.

Tom mentioned our rate cases in North and South Carolina and let me just give you a little bit of additional information in terms of the timeline that we see for both of those. In North Carolina, we are currently in the discovery phase and data requests are being fielded and answered by our folks. On the 16th of August, intervener testimony in the North Carolina case will be due and our hearing in North Carolina is scheduled for the 6th of September. And as Tom mentioned, we would expect rates then to go into effect on November 1st, the first day of our fiscal 2006 year.

Along with the North Carolina general rate case proceeding, we also have an acquisition proceeding associated with acquiring the remaining 50% of Eastern North Carolina that we do not own. A hearing in that case is scheduled for June 23rd.

In South Carolina, we will be filing – electing to file under the newly enacted Rate Stabilization Act and so the schedule that I give you is the first time for us to go through this sort of process, but we will file with the South Carolina Commission on June 15th. On July 15th, interested parties may comment and the regulatory staff in South Carolina will file their comments on September 1st. On September 15th, interested parties again have an opportunity to comment and we would expect a commission order on October 15th with the new rates going into effect.

As I said earlier, this is the first time for us to go through this – first time for anybody to go through this. Following the new rates going into effect, there is an opportunity for any aggrieved party to file a comment or alternative recommendation. That would have to be done by the 15th of November. If indeed that were to happen and we really don't know what will happen there, the commission could issue a different order. And if they do, then new rates would go into effect May 1, but would be retroactive to November 1 of our 2006 fiscal year.

So there's a fair amount on our plate in the regulatory arena. Pleased with the results for the quarter and for the first six months of the year, and generally have ourselves busy on the regulatory front. Probably one of the most important things and I failed to mention that we have requested of the North Carolina Commission is to introduce a conservation tariff, which allows us to decouple the recovery of our margin in North Carolina from the consumption patterns of our customers. This is a great opportunity for us to be able to align ourselves with our customers in terms of fostering conservation along our system while continuing to provide opportunities for customer growth, as mentioned by Frank earlier.

So, there are a couple of other similar type tariffs in place throughout the United States, but we're very pleased with the way we have constructed ours. It's similar to two others in the country and we're hopeful that we can bring that to a successful conclusion in our North Carolina case.

And with that, I'm going to turn it over to Kevin O'Hara.

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

Thank you, Dave. I am going to cover our second quarter earnings from our JVs, including Cardinal Pipeline, Pine Needle LNG, SouthStar, and I'll also provide a briefing on our Hardy project. And the earnings that I will cover are Piedmont's share of earnings from these joint ventures.

On Cardinal Pipeline, this is our North Carolina interstate pipeline joint venture, of which Piedmont has a 21.5% ownership interest. In the second quarter of '05, our earnings are \$280,000 versus \$266,000 in the second quarter of last year. Year-to-date, '05 earnings are \$584,000 versus 550,000 for fiscal year '04.

Pine Needle LNG is our FERC-regulated 4 Bcf interstate LNG storage facility in Guilford County, North Carolina. Piedmont has a 40% interest in Pine Needle and in the second quarter of '05, our earnings were \$582,000 versus 565,000 in the last – in the second quarter of last year. And year-to-date, our earnings are \$1.2 million versus the same amount \$1.2 million for fiscal year '04.

SouthStar is our retail marketing joint venture with AGL Resources. Piedmont has a 30% ownership interest. We share the earnings at 25%. And in the second quarter of '05, we had earnings of \$8.3 million versus \$6.6 million for the second quarter in 2004. Strong retail pricing with SouthStar there to explain the variance and that translate on a year-to-date basis in '05 earnings, at \$11 million versus \$10 million for fiscal year '04.

On the Hardy Storage project, this is our joint venture, 50-50 joint venture between Piedmont and Columbia Gas Transmission to design and build and operate 12.4 Bcf natural gas storage facility in Hardy County, West Virginia. We filed for a FERC certificate on April 25th, that filing provided for a project with \$122 million of costs, 70/30 debt/equity capitalization and 14% ROE. We do expect to get our certificate early fall in September, October timeframe and we're going to operation in April of '07.

With that, I'll turn it back to Kim Cocklin.

Kim R. Cocklin, Senior Vice President, General Counsel, and Chief Compliance Officer

Thank you, Kevin. Bill, I believe we're ready for the Q&A session.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions]. The first line we'll open is David Schanzer with Janney Montgomery. Please go ahead.

<Q – David Schanzer>: Hi. Good afternoon. Dave Schanzer here. A couple of questions. You indicated that you are basically staying with the guidance that you had and you also indicated that in the quarter, basically electric generation made up for some of the shortfall in basic business – retail business. Is that expected to be pretty much the case going forward or do you think it will come back into balance for the last two quarters? I'm trying to get some color, as to how you think the rest of the year will roll out?

<A – David Dzuricky>: Dave, thanks for your question. The best I can tell you at this point in time is we've already given all the color we can give you in terms of providing reiteration of guidance in our press release related to the second-quarter results. To give you any more than that with this limited group I think would be troublesome for us. But the fact of the matter is we have reaffirmed guidance in our press release dated June 7th.

<Q – David Schanzer>: Okay. Well, maybe you can answer this question. Given the budget that you had for the number of connects for the year, do you think – for new customers, do you think that's pretty much in line with what your expectations will be – were when you made them?

<A – Franklin Yoho>: When we look at new customer connects, we look from a historical basis. We're very pleased with the strong success we've had especially in the housing market, and our success in that housing market and the markets we serve. So relative to that, all I can say is we are very pleased that the housing market is still strong and we're still very successful in attaching those homes that are constructed.

<Q – David Schanzer>: But you couldn't comment whether you're on budget or not?

<A – Thomas Skains>: Dave, this is Tom Skains. There obviously – our customer growth numbers are obviously coming in greater than they were last year. We're very pleased with that and expect that trend to continue for the rest of the year.

<Q – David Schanzer>: Okay.

<A – Thomas Skains>: And just color – some more color around our business, again without attempting at all to comment on quarterly influences. In our guidance for the rest of this year, we do expect continued competition in the Number 6 resid markets. We do expect continued customer conservation in response to higher natural gas prices. So those are things that we've taken into account in the business conditions that we face for this year's guidance. And that was always included in our original guidance as well.

As far as the power generation market is concerned, we talked about this in the past. The way we structure our contracts with the large power generation customers, we build pipeline facilities and basically negotiate special contracts for the transportation of gas to those facilities. Those special contracts are approved by the state commissions and are on file with them and generally provide straight fixed variable type monthly charges and we don't have margin rates that apply to their throughput. So when we see increased volumes of deliveries to industrial markets, we don't generally receive any increase in margin associated with that. All of the margin we collect is fixed under the contract – delivery service itself. So, hopefully that just provides you some additional dynamics around the business environment that we're operating in. Again, we do not provide quarter-to-quarter guidance.

<Q – David Schanzer>: No, that's okay. I just wanted to get a little idea of how it would roll out. The other question I have was with regard to SouthStar – the strong retail pricing that you indicated that was the difference in this quarter. Is that something that's likely to continue or is that just too uncertain at this point?

<A – Kevin O'Hara>: We expect going forward that SouthStar's pricing strategies are going to remain the same. We have experienced this over the last two or three years with some of the fluctuations in the cost of gas and SouthStar has been able to take advantage of those fluctuations in their pricing strategy. So, and most of that happens around the first or second quarter. But it ought to stabilize as we go forward through the rest of our fiscal year.

<Q – David Schanzer>: Okay. Thanks.

Operator: The next line we'll open is Mark Levin with Davenport & Company. Please go ahead.

<Q – Mark Levin>: Gentlemen, just to sort of dovetail the first question, is it fair to suggest that the continued competition from the Number 6 resid market and then customer conservation, that those are the two key factors that would lead you either to the lower end of your guidance versus the higher end of your guidance? Or are there other swing factors that would dictate where you fall?

<A - David Dzuricky>: There's probably a million things that could push you one way or the other. The fact of the matter is, Mark, and nice to have you on the call, there's only 7 cents a share spread from the bottom to the top of our guidance. So when we reaffirmed it, we recognized that we were dealing with a fairly tight range of guidance anyway. But as with any company in any industry, there is many, many variables; it can go either way. And all I can tell you at this point is we have reaffirmed that range of 7 cents from \$1.23 to \$1.30.

<Q – Mark Levin>: Okay, fair enough. Second question has to do with interest expense. Can you remind me what percentage of your debt is fixed versus variable? And then as a follow-up, what the sensitivity might be to let's say a 100 basis point change in interest rates?

<A - David Dzuricky>: Mark, all of our long-term debt is fixed. The only interest rate exposure that we have is in our short-term debt. And our short-term debt varies significantly day-by-day and across the month. Our treasurer optimizes our situation in regard to our cash management. We're very pleased with that performance and I can tell you this – interest rates themselves are up about 100 basis points, 110 basis points over last year. So we have absorbed that kind of an increase in our short-term borrowing costs on a year-to-year basis.

<Q – Mark Levin>: Great. Thank you.

Operator: [Operator Instructions]. We have nobody queuing up at this time. Please continue with your presentation.

Kim R. Cocklin, Senior Vice President, General Counsel, and Chief Compliance Officer

I think that that's going to conclude our session. Tom?

Thomas E. Skains, Chairman of the Board, President and Chief Executive Officer

Yes, thank you, Kim. And again thank you all for calling in. We appreciate you following our company and your interest in our company and look forward to chatting with you at the end of the next quarter. So good afternoon to all and have a great summer for those of you who are going to take some time off. Bye-bye.

Operator: Ladies and gentlemen, this teleconference will be available for replay beginning today at 6 p.m. and running through June 27th. You may access the AT&T Executive Playback Service at any time by dialing 800-475-6701. International participants may dial 320-365-3844 and your access code is 784202.

Again, the toll free number is 800-475-6701. International is 320-365-3844 and your access code is 784202. That does conclude your teleconference for today. Thank you for your participation and for using the AT&T Executive Teleconference. You may now disconnect.

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