El Paso Electric Co.

Moderator: Steven P. Busser
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9:30 am CT

Operator: Good day, everyone and welcome to the El Paso Electric Company 1st Quarter 2013 Earnings conference call. Today's call is being recorded. At this time, I'd like to turn the conference over to Mr. Steve Busser.

Steven Busser: Thank you, Shelly and good morning everyone. Thank you for joining the El Paso Electric Company 1st Quarter 2013 Earnings conference call. Also, on the call with me today I have our CEO, Tom Shockley, and our CFO, David Carpenter. Today we will provide an update on our 1st Quarter 2013 performance and we will discuss our key operating results.

Before we get started, I would like to cover some items that will be pertinent to our call. You should have a copy of our press release and if you do not, you can obtain one from our website on the Investor Relations page. We currently anticipate that our 1st Quarter 2012 Form 10-Q will be filed with the Securities and Exchange Commission (SEC) on or before May 10, 2013. Additionally, our 2013 Annual Shareholder Meeting is scheduled for May 9th at 10:00 a.m. here in El Paso.

Please call our Investor Relations department if you have any inquiries or require further information. A replay of today's call will be available shortly after our call ends and will run through May 15th. The details as it relates to the replay are disclosed in our press release.

I'd now like to cover the safe harbor provisions before I turn the call over to Tom.

On page 2 of our presentation, you will see our safe harbor statement. In summary, our comments and answers to your questions may include forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements, involve known and unknown risks and other factors which may cause the Company's actual results and future periods to differ materially from those expressed here. Any such statement is qualified by a reference to the risks and factors discussed in the Company’s SEC act filings. Our 10-K and other SEC filings contain our forward-looking statements and also lay out the risk factors that should be considered. These filings may be obtained upon request from the company, on our website, or from the SEC.

The Company cautions that the risk factors discussed in these filings are not exclusive and we do not undertake to update any forward-looking statement that may be made from time to time by or on behalf of the Company. These statements, especially those made during the question and answer section of the call, are subject to risks and uncertainties that are difficult to predict.

Now I'd like to turn the call over to Tom Shockley.

Thomas Shockley: Thanks, Steve. As you can see on slide number 3 that you've got, we had earnings in the 1st quarter of $0.19 per basic share compared to 2012 when we earned $0.08 per basic share. Later, David Carpenter will step you through in more detail and go through the reasons for those changes. Also, in the 1st quarter we were excited to finish the construction of our Rio Grande Unit 9, which is an 87 megawatt aero-derivative gas turbine. We are in the final stages of testing it and expect it to go commercial operation later this month. So that's an exciting addition to our power plant supply.

For the rest of the year we will be focused on, you can see on page 4 that we will be focused on advancing the construction of our new power plant in East El Paso. It's going to be called the Montana Power Station and it will have ultimately four 87 megawatt aero-derivative type gas turbines, so it will give us a lot of capability to respond rapidly to any changes in our load needs and we're excited to have those as part of our fleet, as well.

We're in the process of finalizing all of the permits that we need. We'll be getting an air permit from the State of Texas, as well as a Greenhouse Gas permit from the EPA. We expect construction to start late this year or early in 2014. So that's an exciting thing. We've already gotten the CCNs for Unit 1 and 2 and we expect to be filing for the CCNs for 3 and 4 later this summer.

The other thing we will be focusing on is our union contract expires in September. So we'll be actively involved in working with our union in getting a constructive settlement for both parties by the end of the summer. So we've got our work cut out for us, but we're excited about things happening in El Paso.

At this time, I would now like to turn the call over to our CFO, David Carpenter.

David Carpenter: Thank you Tom and good morning everyone. I would like to start on slide 5 of our presentation where you will see a summary of our first quarter key earnings drivers. For the quarter, we reported net income of $7.6 million or $0.19 per basic share compared to the first quarter of 2012 results of $3.3 million or $0.08 per basic share. We are pleased to report robust growth in retail non-fuel base revenues, which grew by 2.2 percent when compared to the prior year. I will discuss the retail sales results for the quarter a little later in my comments. The increase in non-fuel base revenue added $0.04 to basic earnings per share. Decreased operation and maintenance expense at our fossil fuel generating plants also added $0.04 per basic share compared to the prior year. The decrease in operation and maintenance expense was primarily due to planned major maintenance that occurred in the first quarter of 2012 on our Rio Grande Unit 8 and Newman Unit 1, generating units, with no major maintenance activity in the current period. Palo Verde operations and maintenance expense also decreased in the first quarter due to the timing of the spring refueling outage in 2012 compared to 2013. The 2012 spring refueling outage for Palo Verde Unit 3 began March 17th, while the 2013 spring refueling outage for Palo Verde Unit 1 did not begin until March 30th. This resulted in decreased Palo Verde operations and maintenance expense in 2013 which added $0.02 to basic earnings per share in the first quarter compared to the previous year.

Allowance for funds used during construction or AFUDC also increased in the first quarter of 2013. Increased construction work in progress for Rio Grande Unit 9 and the new Montana Power Station accounted for most of the increase in AFUDC.

AFUDC capitalization increased first quarter 2013 earnings by $0.02 per basic share, compared to the same period in 2012. Offsetting the previously mentioned increases, net income for the first quarter compared to the same period last year was negatively affected by an increase in administrative and general expenses, which resulted in a decline in basic earnings per share of $0.03. The increase in administrative and general expenses was primarily the result of increased outside services. Also, contributing to the increase in administrative and general expenses was increased benefits expense due to the significant forfeiture of employee stock awards for previous executive officers in 2012, with no comparable activity in 2013.

Now turning to slide 6, we detail by customer class, the change in retail revenues and megawatt-hour sales for the first quarter of 2013 and the percentage change over the comparable period in 2012. As can be seen on this slide, the increases in megawatt-hour sales and retail non-fuel base revenues to residential and other public authorities resulted in the increase in total retail non-fuel base revenue. Megawatt-hour sales to residential customers increased 7.7 percent and megawatt-hour sales to public authorities increased 4.5 percent in the first quarter of 2013 compared to the first quarter of 2012. Favorable weather and growth in usage per customer in the current quarter versus the prior year accounted for the sales increase to residential customers. In terms of weather for the first quarter, heating degree days increased by 15.4 percent when compared to the same period in 2012 and were 9.7 percent greater than the 10-year average. The increase in sales to other public authorities reflects increased sales to new customers and expanding loads at Fort Bliss and other large customers.

Non-fuel base revenues for both small and large commercial and industrial classes declined primarily due to reduced rates for our Texas customers in these classes as a result of the 2012 Texas rate case settlement.

As you can see on slide 7, the rate decrease for Texas customers which took effect on May 1, 2012 as a result of the 2012 Texas rate case settlement decreased non-fuel base revenues by almost $2.5 million in the first quarter of 2013 compared to the same period last year. This decrease primarily affected small and large commercial and industrial customers. The rate decrease was offset by the affects of colder weather and increased heating degree days in the first quarter of 2013, which we estimate increased the quarterly retail non-fuel base revenues by just over $800,000. In terms of customer usage and growth, we estimate that retail non-fuel base revenues grew by just over $4.0 million in the first quarter of 2013 compared to the first quarter of 2012. In summary, we were pleased with the $2.4 million increase in retail non-fuel base revenues we experienced in the quarter.

Now turning to slide 8, we are reiterating our 2013 earnings guidance range of $2.20 per basic share to $2.60 per basic share. The first quarter represents less than 10 percent of our earnings guidance for 2013 and there were not any significant events in the first quarter which would affect our 2013 earnings guidance. As a result, we are maintaining the earnings guidance issued earlier this year.

Finally, just a quick update on the regulatory front. We still anticipate that we will file for rate increases in early 2015 to reflect the Montana Power Station in our rate base.

This now concludes our first quarter 2013 earnings presentation and I will now open up the call for questions.

Operator: Thank you, if you would like to ask a question, please signal by pressing star 1 on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star 1 to ask a question. And we'll pause for just a moment to allow everyone an opportunity to signal for questions.

We'll take our first question from Neil Mehta with Goldman Sachs.

Neil Mehta: Good morning.

Steven Busser: Good morning.

David Carpenter: Good morning.

Neil Mehta: I'm thinking about the rate case timing for 2015 with 2016 implementation. Will that only be in Texas as they stand right now, or could you file in New Mexico as well?

David Carpenter: I think as we have looked at the timing of the rate case further, we believe that we will likely file rate cases in both Texas and New Mexico. Because Texas generally is a bigger impact than New Mexico, we'd probably try to file that first and follow shortly thereafter with a New Mexico case.

Neil Mehta: Would you file both in 2015 or were you thinking about New Mexico a potential filing in the 2014 time?

David Carpenter: I think we would file both in 2015, probably on a pretty tight time schedule for both of them.

Neil Mehta: And how do you think about the trajectory of AFUDC? Is there going to be an up-lift in 2014 as you continue to build out Montana too? And then how much of a decrease should we anticipate in 2015 as that plant goes online?

David Carpenter: Clearly, I think there will be an increase in 2014 and then once the Montana plant goes in service in December 2014, you'll see a decline. Then when the second unit of the Montana plant goes in service, probably around May of 2015, you'll see another decrease. So we would expect 2014 to be a little bit higher than 2013 and 2015 to be a little bit lower, with the decline from 2014.

Neil Mehta: And last question is around O&M. O&M decreased in the quarter. Was the first quarter just an unusually high period for outages? Should we assume that the first quarter of 2012 meaning 1Q 2012 last year -- could we assume this year's first quarter is the right run rate? And then what type of O&M growth do you expect for the balance of the year?

David Carpenter: We think that for the balance of the year, O&M will be fairly flat compared to last year. We'll pick up a little bit of maintenance in the second quarter, and the Palo Verde maintenance will occur in the second quarter, of which some of that occurred last year. So we expect Palo Verde to catch up in the second quarter and we also expect that we'll see some catch-up in the fossil fuel plant maintenance and O&M in the second quarter and further this in other quarters this year, probably more in the fall.

Neil Mehta: Thank you very much.

Operator: We'll take our next question from Anthony Crowdell, with Jefferies.

Anthony Crowdell: Good morning, two quick questions.

First, I want to know how much of the rate refund you have left to apply to customers or our book. And the second thing is, is the higher administrative and general expense that you said was a negative $0.03 headwind for the quarter, and is that listed in other operating expenses or in some other section?

David Carpenter: Anthony, let me answer the first part. We think there is probably about $800,000 left in April for the rate decrease and then May was the start of a rate decrease last year. So from May on, it will be on comparable rates this year and last year again. Can you repeat the second part of your question?

Anthony Crowdell: Sure. I was just wondering where in the income statement you have booked the higher administrative and general expense. I think you said it's a negative $0.03 headwind for the quarter. Is that in other operating and maintenance expense?

David Carpenter: Yes.

Anthony Crowdell: Okay, great.

David Carpenter: Yes. It's in your non-Palo Verde operation and maintenance expense.

Anthony Crowdell: Got it.

Operator: Thank you.

If you find your question has been answered, you may remove yourself from the queue by pressing star 2 and its star 1 to ask a question.

We'll take our next question from Maury May, with Wellington Shields.

Maury May: Good morning, folks. Good quarter.

Steven Busser: Hi Maury.

Maury May: I want to get back to AFUDC going forward for the next few years. I recall about a year ago Steve, I think it was you that actually gave us the projected numbers of AFUDC for several years hence. I was wondering if you could do that again, please?

Steven Busser: Yes, I think David did a pretty good job. I don't have the exact number in front of me, Maury, but I think David did a pretty good job of walking through AFUDC. We'll see an increase relative to this year of probably about 10-15 percent over what we're expecting in 2013 and we'll see about a 10-15 percent increase in 2014.

Maury May: Okay. What are you expecting in 2013?

Steven Busser: Our expected AFUDC in 2013 is right at about $19½ million.

Maury May: Okay.

Steven Busser: We expect a bit of an increase in 2014 and then as David mentioned, we'll see that tail off and probably get back probably to around the 2012 levels, if you're just looking to an approximate level.

Maury May: Okay.

Steven Busser: Beyond that, I don't think we've really given any guidance.

Maury May: Okay. Now you said 2014 would be up about 10 percent from 2013.

Steven Busser: 10 to 15 percent, yes.

Maury May: Okay, and could you remind us what the 2012 levels were?

Steven Busser: Yes, 2012 was about $15 million.

Maury May: Okay, so you're saying 2015 then would return to the 2012 levels.

Maury May: Okay.

Steven Busser: Probably around that range, Maury, I don't have an exact number.

Maury May: Okay. Good.

Maury May: Second question has to do with cash. You ended the first quarter with $43.7 million in cash and I was wondering, how that was created because you used to have big cash piles, but then you bought back stock and of course you are building now. So where did the $43.7 million come from?

David Carpenter: Yes, Maury.

Maury May: And what are you going to do with it?

David Carpenter: Yes, we issued $150 million of Senior Notes in December

Maury May: Right. Okay.

David Carpenter: Basically what we've been doing is working that. We really kind of pre-funded construction for 2013 and that was about $43 million at the end of the first quarter. We'll see that decline some more once we get into the summer we'll probably generate a little bit of cash and we think that by the end of the year we'll be fairly flat and maybe borrow a little bit. Then of course when you look at the construction expenditures in 2014 being over $325 million or around $325 million, we'll need to go out and borrow some more money in 2014 to finance our construction program.

Maury May: Okay. You really have, what, several hundred thousand shares left in the share repurchase program. I guess you really don't see you all buying any of that, do you?

David Carpenter: No, we really don't, not this year or for the next couple of years, probably.

Maury: Okay, and then my final question has to do with guidance. Despite the, rather buoyant first quarter, you're maintaining your guidance at $220 to $260, which is kind of a wide range. I was wondering whether you could give us some color on that guidance and whether you think you might be in the middle of the guidance, upper end, lower end that kind of thing.

David Carpenter: Well I think right now our expectations are that we would be close to the middle and assuming normal conditions and in our guidance range always reflects, I think we've mentioned before that probably about half of our guidance range is the potential for weather-related changes that if we have a really hot summer we'd probably move toward the upper end of our guidance, if we have a milder summer we move to the lower end.

But the summer weather really is a significant factor, much more significant than the weather in the first quarter on our overall earnings. So until we get through the summer, we probably won't tighten our guidance. And the other factors are just variances in O&M

and our revenues from Palo Verde Unit 3 are the primary drivers for changing the guidance going forward.

David Carpenter: Again, we won't have a more detailed analysis on that until later in the year.

Maury May: Okay, great.

Steven Busser: Hi Maury, this is Steve. I want to just clarify an answer that I gave you on the AFUDC issue.

Maury May: Ok

Steven Busser: I think I led you to believe that 2015 would go back to 2012 levels. What I meant to say is 2015 will go back to 2013 levels. So I apologize.

Maury May: Right. Oh, okay, good. That's a little bit higher. Okay. Thanks, Steve. Thanks, David.

Operator: We'll take our next question from Michael Klein, with Sidoti and Company.

Michael Klein: Hi, good morning.

David Carpenter: Morning.

Steven Busser: Good morning, Mike.

Michael Klein: Real quickly and I apologize if you answered this already. Just looking at the variance between sales growth and population growth, obviously sales growth was heavily driven by weather, but the population growth tailed off. Is this sort of a run rate to assume going forward, or was it just seasonality? Or how can you guys characterize that?

David Carpenter: We think that to a large extent that it's probably primarily seasonality. There is a small portion of it related to understated growth rate because we've had a number of customers that have been consolidating their accounts.

So while we really haven't had the number of customers still there, the load is still there, because they've consolidated accounts you've had a decline that is primarily in the small commercial class where they've consolidated accounts.

So if they have 10 different service loads and they connect and they now list that as one load, it declines our customers by nine. And so we've had a little bit of that, and I think you see that primarily in the small commercial class. And then the other thing that we say when we had Dr. Gilmore speak at our analyst day in February he mentioned a slowdown in the economy in the first half of 2013 and then a pickup in the second half.

And what we're really seeing is maybe a little bit of a slowdown in the first half, but when we talk to our construction people that are out working on setting up new subdivisions and new loads; they tell us that they're busier than ever. So our expectation is that we may continue to see a little bit sluggish customer growth in the second quarter. And right now, our expectation is that it probably picks up in the third quarter.

Michael Klein: Okay. That's helpful. You still think that 1 or 1 1/2 percent growth on an annual basis is achievable or realistic?

David Carpenter: We think so.

Steve Busser: Customer growth. Right.

Michael Klein: Yes. Okay, great. That's all I had. Thank you very much.

David Carpenter: Thank you, Mike.

Operator: We'll go to Tim Winter, with Gabelli & Company.

Tim Winter: Good morning, congratulations on the quarter. I just wanted to follow up a little bit on the health of the service area. You had talked about the military base expansion maybe slowing in 2013 and a number of sort of developments like baseball stadium and a medical facility. Could you just give us an update on all of that?

David Carpenter: Sure. We're continuing to see expenditures made at Fort Bliss and we're not really seeing troops added. Steve can correct me here, I think there's about 3,000 troops that are still deployed and that are supposed to be coming back later this year, but what we are seeing is continued construction of housing at the base and other facilities the hospital complex, I think, has now started physical construction. And so we'll continue to see some pickup from that. We're also seeing some construction activity related, well, a lot of construction activity related to construction of homes and apartments in El Paso and we're also continuing to see the expansion of the medical facilities. They're proposing a $25 million construction and I think this doesn't begin until 2014 for its Medical Center of Americas, which is a Biomedical Research Park, associated with Texas Tech University Medical School, and I believe that's slated to begin construction in 2014. Anything else, Steve?

Steven Busser: We had a bond levy that was passed in late 2012 for about $475 million of Quality of Life bonds. They've recently demolished City Hall, which is where the new baseball stadium will go and so construction is underway to begin that effort and there's other committees and things like that at the city level that are trying to determine exactly how they're going to spend those dollars for other projects around the city.

David Carpenter: Yes, and one other thing I just forgot about there. We're continuing to see a large amount of money being spent on highway construction in El Paso as they kind of build out the highway system to help support the growth that we've been seeing.

Tim Winter: Okay, great. Thank you.

Steven Busser: Thanks, Tim.

Operator: There are no further questions at this time.

Steven Busser: Thank you, Shelly. And thank you all who joined us today. We appreciate your attention.

Have a great day.

Operator: Thank you. This concludes today's presentation. We thank you for your participation.