Challenges in Energy Financing

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2009 Investor-Owned Utility Sector Outlook

- Industry Outlook is Stable
- Fundamentals expected to remain intact near-term, although rising business and operating risks may stress credit profile longer term
- State regulators continue to grant timely recovery of prudently incurred operating costs and capex
- Key financial metrics likely to deteriorate modestly over next 12 to 18 months, but utilities have adequate time to bolster financial strength

Key Challenges Facing Investor-Owned Utilities

- Potential for significant environmental legislation
- Sizeable infrastructure investment plans
- Regulatory risk over the pace and amount of rate relief, especially in a recessionary environment
- Protracted economic pressures may increase intensity of business and operating risks
- Missed opportunity to issue equity may prove costly
- Maintaining unfettered access to capital markets key

Does the sector need equity?

Historical Stock Prices - October 24

	2004	2005	2006	2007	2008
AEP	32.32	37.20	41.64	46.51	30.98
BKH	28.11	40.88	34.75	41.98	24.32
D	31.76	38.64	40.40	43.25	35.14
DUK	23.74	25.94	31.57	18.65	15.63
DYN	4.77	4.46	6.20	8.47	2.54
EIX	29.83	42.09	44.03	54.52	32.39
ETR	64.45	70.30	85.21	114.85	79.72
EXC	39.35	52.76	62.26	76.44	48.55
FE	41.07	46.70	59.32	66.08	49.18
FPL	34.40	43.48	48.17	61.89	43.20
MIR	na	na	29.68	41.30	15.09
PEG	20.76	31.59	30.56	44.65	27.64
PNM	23.24	25.33	28.46	23.64	8.42
PPL	25.80	30.69	35.12	47.82	29.33
RRI	10.50	12.81	12.98	25.20	4.86
SRE	34.34	42.88	53.24	58.56	38.11
TEG	na	54.16	53.14	51.28	44.12

Commercial Paper Markets Have Been Choppy

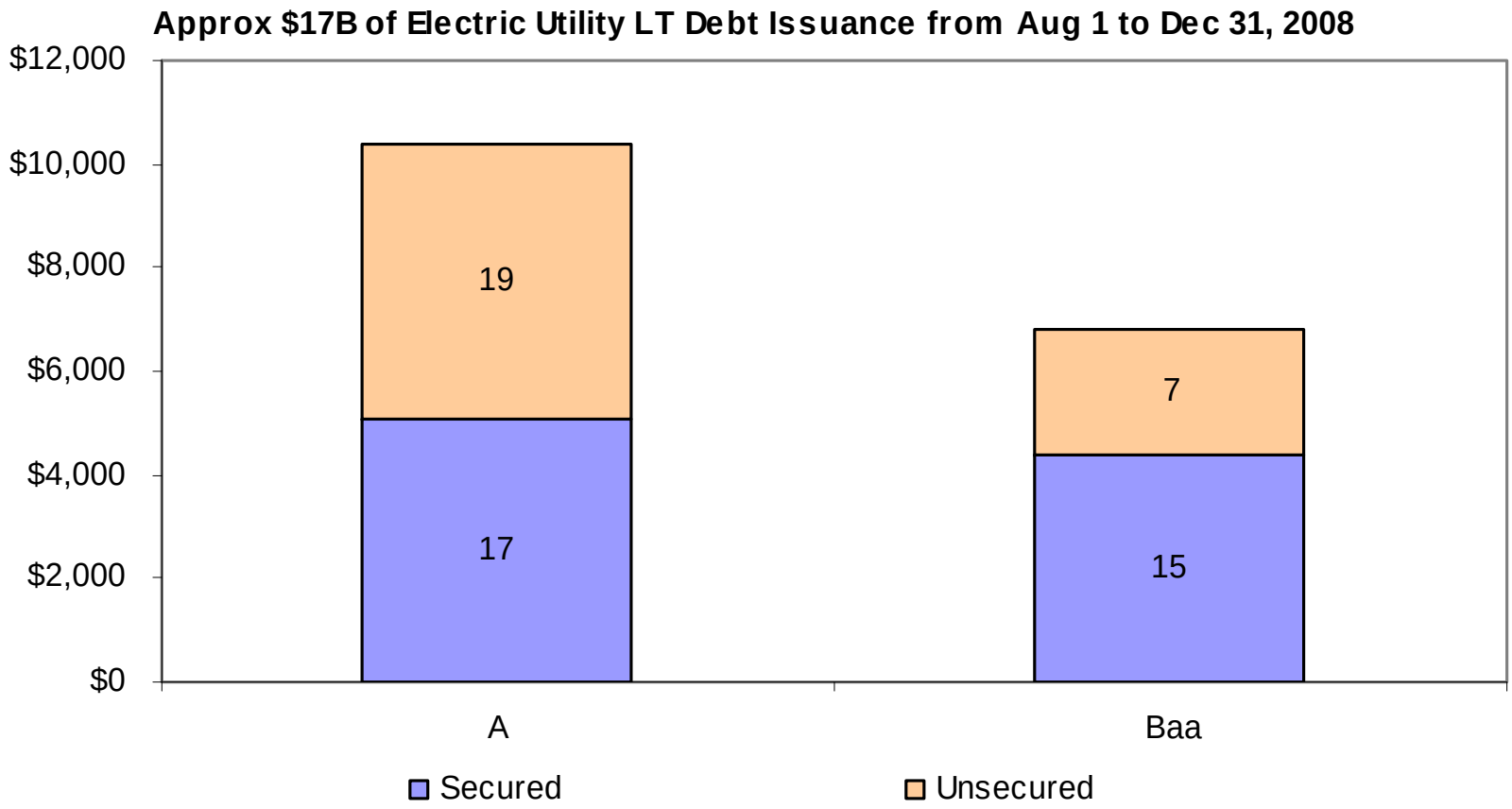
- Flight to quality has helped some Prime-1 rated utility issuers
- Federal Reserve's Commercial Paper Funding Facility (CPFF) has helped the Prime-1 CP market
- In late 2008, many utilities forced to limit CP maturities to overnight or only a few days
- Prime-2 issuers were the most severely affected, with some drawing on bank credit facilities

Publicly Disclosed CP Backstop Facility Draws

Major Utility Commercial Paper Issuers Drawing on Bank Credit Facilities in 2008

Utility	CP Rating	Draw Amount ($MM)
American Electric Power	Prime-2	$1,400
Duke Energy	Prime-2	$1,000
Progress Energy	Prime-2	$600
Southern California Edison	Prime-2	$1,800

IG Utilities Still Have Bond Market Access . . .



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. . . But At Sometimes Higher Spreads

Issue Date	Issuer	Type	Rating	Size $mm	Coupon	Term	Spread
10/1/2008	Interstate P&L	Sr. Unsec.	A3	$250	7.25%	10 yr	358
10/16/2008	Pacific Gas & Electric	Sr. Unsec.	A3	$600	8.25%	10 yr	456
9/8/2008	Consumers Energy	FMBs	Baa1	$350	6.13%	10 Yr	246
10/15/2008	Ohio Edison	FMBs	Baa1	$25	8.25%	10 yr	456
9/3/2008	Oncor Electric	FMBs	Baa3	$550	6.80%	10 yr	313
10/20/2008	Illinois Power	FMBs	Baa3	$400	9.70%	10 yr	609

Adequate Liquidity Biggest Near-term Challenge

- Credit facility expirations loom, posing a significant concern if markets do not improve
- Major institutions exiting commodity markets is an intermediate-term risk
- Sector's substantial negative free cash flow requires unfettered capital markets access
- Utilities need to consider alternative sources of liquidity to replace banks

Utilities Benefited From Favorable Credit Markets

- Traditional bank financing is highly relied upon by industry for working capital and CP backstop
- Utilities have taken advantage of competitive banking conditions in recent years
- Most have negotiated favorable terms and conditions for their existing credit facilities
- Utilities with multi-year facilities out to 2011 and 2012 are in advantageous position to weather the credit and liquidity crisis

But Pendulum Swung in the Other Direction

- Unsettled financial market conditions reshaped the banking sector during 2008
- Bank failures, government interventions, and mergers have reduced the number of banks
- Banks remaining are constrained in their ability and inclination to provide credit to utilities
- Most will be focused on restoring their own balance sheets over the near-term

Consequences May Be Profound For Sector

- Credit facilities will have shorter average tenors
- There will be substantial increases in credit facility pricing
- Pricing may be tied to more volatile market indicators, such as CDS spreads
- Conditionality may increase with more restrictive financial covenants
- Credit facilities are more likely to be secured

Utilities with Near-term Maturities Vulnerable

- Utilities with credit facility maturities in 2009 and 2010 are most affected
- They will likely have to address renewal needs while bank markets remain constrained
- Less time to develop alternatives to traditional bank financing
- Alternatives include asset backed financing, vendor financing, or lien based hedging, etc.
- Smaller credit facilities can be expected

Retreat by Financials Could Impact Hedging

- Will market dislocation of financial institutions affect utility hedging programs and strategies?
- Utilities will have fewer counterparties to trade with
- Bid-ask spreads will widen
- Hedging transactions likely to be shorter-dated
- Higher cost of credit
- Greater use of commodities exchanges
- New terms of expiring PPA's may be more onerous

2009 Public Power Utility Sector Outlook

- Credit Outlook is Stable
- Based on monopolistic positions as essential service providers and their ability to recover costs through rate-setting process not subject to regulation
- However, recession pressures could reduce demand
- Lower demand could weaken debt service coverage or liquidity if rates are not raised to compensate
- Weakening local governments could lead to more general-fund transfers from public power utilities

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Question & Answer

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