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GXP - Q1 2015 Great Plains Energy Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Great Plains Energy first-quarter 2015 earnings conference call. (Operator Instructions). As a reminder, this call is being recorded.

I would like to introduce your host for today's conference, Lori Wright, Vice President of Investor Relations and Treasurer. Ma'am, you may begin.

Lori Wright - Great Plains Energy - VP IR & Treasurer

Thank you operator and good morning. Welcome to Great Plains Energy's first-quarter 2015 earnings conference call. Let me begin by introducing Terry Bassham, Chairman, President, and Chief Executive Officer, and Jim Shay, Senior Vice President Finance and Chief Financial Officer, who will provide an overview of our first-quarter 2015 results. Scott Heidtbrink, Executive Vice President and Chief Operating Officer of KCP&L, is also with us this morning, as are other members of our management team who will be available during the question-and-answer portion of today's call.

I must remind you of the inherent uncertainties in any forward-looking statements in our discussion this morning. Slide 2 and the disclosure in our SEC filings contain a list of some of the factors that could cause future results to differ materially from our expectations.

I also want to remind everyone that we issued our earnings release and first-quarter 2015 10-Q after the market closed yesterday. These items are available along with today's webcast slides and supplemental financial information regarding the quarter on the main page of our website at GreatPlainsEnergy.com.

With that, I will now hand the call to Terry.

Terry Bassham - Great Plains Energy - Chairman, President, CEO

Lori, good morning everybody. I'll start with Slide 4 this morning. On our call, we'll discuss our first-quarter results and progress on the environmental upgrade at La Cygne and the completion of the first project at Transource. We'll also provide an update on KCP&L's rate cases in Missouri and Kansas.



Yesterday, we announced first-quarter earnings of \$18.5 million, or \$0.12 per share, compared to \$23.4 million, or \$0.15 per share, in 2014. Key drivers for the quarter include favorable operations and maintenance expense and a return to more normal weather with heating degree days 13% below the first quarter of 2014, when we experienced extremely cold temperatures from the polar vortex. We also affirmed our 2015 EPS guidance range of \$1.35 to \$1.60. Jim will discuss more details on the quarter in his comments.

On the operations front, the La Cygne environmental upgrade has successfully completed its in-service testing and we expect the final cost to be below budget. This construction project, one of the largest in our Company's history, has proceeded extremely well and is a testament to our ability to successfully execute on large projects.

The refueling outage at our Wolf Creek nuclear unit is complete and it returned to service earlier this week. While the unit was down, we took the opportunity to make modifications to the essential service water system. These upgrades are necessary to meet government mandates regarding aging infrastructure and allow us the continued safe and reliable operation of Wolf Creek.

These investments at La Cygne and Wolf Creek represent a significant portion of our projected 4% to 5% rate base growth in 2014 to 2016.

We are also pleased that our Transource joint venture completed the first of two projects under development in the Southwest power pool region. The Iatan to Nashua transmission line was energized last month ahead of schedule and under budget. The 31-mile 345 KV line extends from KCP&L's Iatan power plant substation to the Nashua substation near Smithfield, Missouri. The line will reduce known transmission constraints on our system, allowing more low-cost generation to benefit the region.

Transource's second project under development in the SPP region, the Sibley to Nebraska city line, is expected to be in service in 2017.

The successful execution of the Iatan to Nashua project demonstrates the combined scale and capabilities of Great Plains Energy and AEP. As the emerging competitive transmission market develops, we believe Transource is well-positioned to compete and deliver innovative solutions.

I'll wrap up with a few comments on KCP&L's rate case proceedings in Missouri and Kansas.

In its direct testimony filed last month, the Missouri Public Service Commission staff recommended a revenue increase range of \$82.4 million to \$91.3 million predicated on a return of equity range of 9.0% to 9.5%. As a reminder, KCP&L's request is for \$120.9 million based on an ROE of 10.3%. Hearings in this case are scheduled to begin the week of June 15 and new rates effective by the end of September.

In Kansas, we requested an increase of \$67.3 million, also based on an ROE of 10.3%. The Kansas Corporation Commission Staff and other intervenor testimony is due next Monday and hearings are scheduled for the week of June 22 with new rates effective early October.

You can find summaries of the rate cases in the appendix of this presentation.

The components of the rate cases are straightforward and we are working diligently to achieve constructive outcomes, that include reducing risk and volatility of our ongoing returns. We remain on plan to deliver our 2014 to 2016 annual earnings and dividend growth targets of 4% to 6%. Increased cash flow flexibility post 2016 will allow for ongoing investment and dividend growth as well.

I will now turn the call over to Jim to discuss our first-quarter financial performance.

Jim Shay - Great Plains Energy - SVP Finance, CFO

Thank you, Terry, and good morning everyone.

I'll begin with Slide 6, which provides a comparison of the 2015 first quarter to the first quarter of 2014. As Terry indicated, our first-quarter 2015 earnings were \$0.12 per share compared with \$0.15 per share last year.



Earnings were favorably impacted by lower O&M expense which was more than offset by warmer weather compared to the first quarter of 2014 and an increase in depreciation and amortization.

The favorable O&M variants included lower operating and maintenance expense at Wolf Creek related to the planned 2014 mid-cycle maintenance outage and a decrease in refueling outage amortization. Lower distribution operating and maintenance expense also contributed to the decline. As we think about the next three quarters, we expect our O&M expenses to increase above the 2014 levels. Consistent with our [2015] (corrected by company after the call) guidance, we expect overall O&M for the full year to increase 3% to 4%, which includes increases in regulatory amortizations and items which have direct revenue offsets. As a reminder, the O&M items with direct revenue offsets include our Missouri Energy Efficiency Investment Act programs. These investments allow us to invest in our customers by providing long-term energy solutions and an ability to generate shareholder returns. We recover program costs and a throughput disincentive for these programs which is included in our gross margin. Our O&M increase for 2015, exclusive of regulatory amortizations and items which have direct revenue offsets, is 1% to 2%.

As we discussed on our 2014 year-end call, AFUDC will decline in 2015 as the La Cygne environmental upgrade and other projects included in our current rate cases move from CWIP to in-service. We will also be impacted by increasing lag from property taxes, transmission costs, and depreciation until new rates are in effect. Lower natural gas prices are negatively impacting off-system sales, which has an earnings impact at KCP&L Missouri where we do not have a fuel clause. In its Missouri rate case, KCP&L is seeking authorization to utilize a fuel clause by the fourth quarter this year, which would mitigate this exposure as we move forward. As a result of these drivers along with the impact of increasing O&M, we expect second-quarter 2015 earnings to be lower than the same period of 2014.

Weather-normalized demand net of the estimated impact of our energy efficiency programs was up 0.1% in the first quarter and in line with our full-year projection of flat to 0.5%. Positive commercial and residential demand was almost entirely offset by lower industrial demand.

We continue to have confidence that our regional economy will remain strong. Positive trends impacting the commercial and residential sectors include February unemployment of 5.9% that is well below the 6.6% rate for our region a year ago and in line with the national rate of 5.8%. Housing remains strong with March year-to-date single-family housing permits at their highest level since 2008.

The first quarter decline in the industrial sector was primarily due to Ford Motor Company's Kansas City assembly plant. The F-150 line was shut down for part of the quarter for retooling to build the new trucks using military-grade aluminum alloy with production resuming in March. This temporary shutdown was expected and we are still comfortable with our overall full-year demand forecast of flat to 0.5%, net of the estimated impact of our energy efficiency programs.

We continue to see Kansas City as a developing automotive center in the United States. Combined with the General Motors plant near our service territory and auto suppliers moving to our region, Kansas City is the second largest automotive manufacturing center in the United States outside of Detroit.

On the capital markets front, we expect to issue long-term debt at KCP&L in the second half of 2015 with no plans to issue equity.

As Terry indicated, we reaffirmed our 2015 earnings-per-share guidance range of \$1.35 to \$1.60. We feel confident in our ability to execute on our financial objectives for the year. The outlook for the Kansas City economy, our history of diligent cost management and track record of achieving constructive regulatory outcomes provides us confidence in our ability to deliver 4% to 6% earnings growth from 2014 to 2016.

Thanks for your time this morning. Terry, Scott, and I would now be happy to answer any questions that you may have.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Ali Agha, SunTrust.



Ali Agha - *SunTrust Robinson Humphrey - Analyst*

My first question, Terry, recently we had a rate case decided in Missouri that set the ROE at 9.53%. Should we use that or assume that is kind of the floor of ROEs to be thinking about as you go through your rate case?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

You know, it's hard for me to say for sure but I certainly would expect that to be kind of the range we would be dealing with. As a reminder, we are at 9.7%, so 9.53% to 9.7% would be a range that I would probably expect to be dealing with. That's probably fair.

Ali Agha - *SunTrust Robinson Humphrey - Analyst*

Okay. And then secondly, assuming constructive rate case outcomes as we think about 2016, should we again think about, in a best case scenario, an aspiration of bringing the regulatory lag down to 50 basis points? Is that again the best case scenario, or would that be different this time around?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

Well, again, we'll have to wait to see how these cases come out and we've asked for several things to help mitigate that pretty dramatically. I think we've traditionally said that 50 to 100 is the kind of target that we are constantly working toward. I certainly think that shoring up our costs in these rate cases is important to get there, and so I don't see anything yet that would cause that to change. Certainly, we are looking and continuing to ask for things that would help make that more consistent year-over-year.

Ali Agha - *SunTrust Robinson Humphrey - Analyst*

Okay. But again, even -- we should still assume there will be some lag even in the best of scenarios?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

If you look at a lower level of growth and a growing service territory, which we have both, then yes. Given years, it could be slightly above or below that range, but in general if you've got some load growth, you are trying to meet new demand, but yet you don't have some of the trackers we'd like to have in the past, which is why we're asking for them now, we would expect to continue to have a little bit of lag as long as we are growing.

Ali Agha - *SunTrust Robinson Humphrey - Analyst*

Got it. And my last question, Terry, just to clarify your comments, the 4% to 6% EPS growth 2014 through 2016, in the past, you had talked about the base being your original 2014 guidance. Is that still the case or should we use the 2014 actual as our starting point?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

It has always worked off the guidance.

Ali Agha - *SunTrust Robinson Humphrey - Analyst*

The original guidance?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

Of 2014 -- in 2014, yes.

Ali Agha - *SunTrust Robinson Humphrey - Analyst*

Got it. Thank you.

Operator

Shar Pourreza, Guggenheim Partners.

Shar Pourreza - *Guggenheim Partners - Analyst*

Can we just get a little bit of an update on Transource and see how the progression there is going? And then I'd be curious to get your viewpoint on how you think the Artificial Island latest order impacts our growth aspirations at least for those type of projects.

Jim Shay - *Great Plains Energy - SVP Finance, CFO*

We really like how we are positioned at Transource for the long-term. We are really active in the SPP, MISO, and PJM marketplaces and those markets have been slower to develop than I think everyone was originally hoping for. But we think they are good, long-term markets for the future.

As we think about Artificial Island, we think that, although we are disappointed that Transource didn't receive Staff's recommendation, we are really starting to see some positive signs that we think the market is going to start to develop and in particular, the fact that non-incumbents are getting an opportunity to participate and are receiving notices to construct. And we also see that, through the competitive process, customers are getting solutions delivered at a lower cost. So, we think we've been at this for a little bit, we like how we are positioned in these markets and we think we are going to be successful.

Shar Pourreza - *Guggenheim Partners - Analyst*

Got it, thank you. And then just it's a little bit preliminary here, but obviously you are asking for some trackers and riders in the rate case. Is there any sort of updates on how settlement discussions are going? And then also, as far as the GRC, if you've fully updated for the deferred taxes that you mentioned on Slide 17?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

Yes, it's a little early to talk settlement. Obviously, testimony is still getting filed. We would expect, as all the testimony gets filed in the next week or so, two weeks maybe I think for Kansas, and in the time for hearings is when a lot of that conversation happens. So we'll be watching for all that to get in. We'll continue to work on ways to make those trackers and riders possible, but we are likely to have to litigate some of those things and not be able to come to a settlement.

Jim Shay - *Great Plains Energy - SVP Finance, CFO*

And Shar, I think part of your question was with us taking some bonus depreciation and the impact that has on deferred taxes, that will be part of our true-up and we're still confident in our \$6.5 billion rate base target after taking those factors into effect.

Shar Pourreza - *Guggenheim Partners - Analyst*

Excellent, excellent. And then just lastly, equity, is there an update on when -- the earliest you could potentially tap?

Jim Shay - *Great Plains Energy - SVP Finance, CFO*

You know, if a strong deferred tax asset position and us not needing to pay taxes until beyond 2020, we shouldn't have any equity needs for the foreseeable future.

Shar Pourreza - *Guggenheim Partners - Analyst*

Excellent. Thanks so much.

Operator

Charles Fishman, Morningstar.

Charles Fishman - *Morningstar - Analyst*

Good morning. I saw the headlines on the Ameren decision, but I'm guilty of not reading the full decision, and I was wondering if you could tell me. Was there anything in the decision that makes you feel better or worse with respect to getting the property tax tracker, the CIPS tracker, and the vegetation tracker for KCP&L Missouri?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

This is Terry. I would say that, certainly, we think we have a strong case in particular about property taxes. We also think we have a good case on the others and are very pleased to at least be making progress on the large asset ask. Certainly given the Ameren order, we've got a little tougher hill to climb maybe to get the riders and trackers that were addressed in the Ameren case, but we've got our own case to make and we'll do that and we'll see where that goes.

Charles Fishman - *Morningstar - Analyst*

Okay. And then my second question was I thought that the low end of your 2015 guidance was driven by a potential outcome of the delay in the La Cygne in service. With La Cygne now being in service, can we expect maybe the low end of that, of your 2015 guidance, to come up a little?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

We've reaffirmed our guidance. And it's based upon -- and that was one of the issues that could affect guidance either way. And it wasn't so much La Cygne as it was rate case timing in general, La Cygne being one piece. We've also got load growth. That's an issue. We've got to manage our costs. We've got several things that could affect that range right now. We are reaffirming the range as we've stated, and update you later in the year. Remember that a large part of our earnings come in the second and third quarter.

Charles Fishman - *Morningstar - Analyst*

But KCP&L's two rate cases are going forward pretty much as you expected at the time you issued guidance?



Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

Yes. At this point, we would expect the schedule for rates to stay in effect.

Charles Fishman - *Morningstar - Analyst*

Okay, thank you. That's it.

Operator

Paul Ridzon, KeyBanc.

Paul Ridzon - *KeyBanc Capital Markets - Analyst*

I was hoping you could give an update on your legislative efforts. It looks like 2015 is not going to be a year where something happens. But are there discussions ongoing about maybe getting something in place in the next session?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

So, I assume, Paul, you are talking mainly about Missouri.

Paul Ridzon - *KeyBanc Capital Markets - Analyst*

Yes, yes, sorry.

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

No, that's okay, because there's obviously things happening in Kansas on occasion as well. But yes, I think we talked about the fact that 2015 wouldn't be a year that we push. We've got rate cases and things going on. We will continue to talk about the legislature, the issues with the legislature. I would tell you that there are occasions when you talk to the legislature and they say you should go to the Commission. Times you go to the Commission, they say it has to be legislative. We certainly have a baseline that we expect to be set this year because of the rate cases in the three large utilities which will allow us to have conversations in January based upon hard facts, and I'm sure we will be having those conversations. It's a little early to say what we will be talking to them about and how we'd structured the 2015 session is not quite over yet.

Paul Ridzon - *KeyBanc Capital Markets - Analyst*

Thank you.

Operator

Brian Russo, Ladenburg Thalmann.

Brian Russo - *Ladenburg Thalmann & Company, Inc. - Analyst*

Could you just remind us the EPS drag you are forecasting in your 2015 guidance related to under-recovery of transmission expenses?

Jim Shay - Great Plains Energy - SVP Finance, CFO

Yes. For 2014, we had drag of about \$0.12, and we expect that to increase in 2015.

Brian Russo - Ladenburg Thalmann & Company, Inc. - Analyst

Okay, and the 50 to 100 basis point lag target that you guys are looking to achieve, does that assume transmission expense is recovered in a fuel clause or does that assume you are just able to manage around that ongoing under-recovery?

Jim Shay - Great Plains Energy - SVP Finance, CFO

Through the rate process, we'll true up transmission costs to the current level. With a transmission in our fuel factor, we would be able to better manage that lag moving forward but without transmission as a fuel factor, there would be some lag, but it should be manageable within the 50 to 100 range.

Brian Russo - Ladenburg Thalmann & Company, Inc. - Analyst

Okay, great. And then just what is your allowed ROE on transmission?

Jim Shay - Great Plains Energy - SVP Finance, CFO

Our allowed is 11.1% through Transource and then our KCP&L and GMO are also at 11.1%. That's for our FERC regulated transmission.

Terry Bassham - Great Plains Energy - Chairman, President, CEO

Those Transource base is 9.8% with the adders. KCP&L is 10.6% with the adders, both equaling to Jim's 11.1%.

Brian Russo - Ladenburg Thalmann & Company, Inc. - Analyst

Got it. Thank you very much.

Operator

Michael Goldenberg, Luminus Management.

Michael Goldenberg - Luminus Management - Analyst

Good morning. My questions have been asked and answered. Thank you.

Operator

Paul Patterson, Glenrock Associates.



Paul Patterson - *Glenrock Associates - Analyst*

I wanted to follow up on Paul Ridzon's question. I wasn't completely clear on the answer or what the cause is that -- could you just elaborate a little bit more as to why the legislation, in your opinion, legislative efforts haven't been fruitful? It wasn't just this year. I think last year you guys were also trying something as well. And you mentioned something about the timing of the rate case. And could you just elaborate a little bit more on that?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

The short answer is that we've been working several years in Missouri on addressing a few issues obviously, and we had our bigger program that we were talking to them about. Candidly, there is at least -- well, the largest user of electricity in the state of Missouri has been opposed to those kind of legislative efforts and we've dealt with that several years in a row. This year, because we had rate cases coming and many of the issues we are talking about would be addressed on a regulatory basis, we talked to the legislature as always, but our expectation was not necessarily that anything would move this year. Ameren has now had a rate case. We'll have a rate case. Empire has a rate case. We'll now have a fresh set of facts, if you will, to talk to legislators about next year. So that was kind of what I was alluding to if that makes sense.

Paul Patterson - *Glenrock Associates - Analyst*

Okay, I think I understand. I guess what I'm wondering is what do you think is going to change in the political environment there? Whether it's a large electric user or whatever the reasons are, how should we, in terms of looking at this and the opportunity for you guys to get legislation, how should we think about the situation potentially changing other than the fact that you guys will have some rate cases in place?

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

I don't know that I could tell you exactly what to expect. What I can tell you is that, if we are unable to continue to get assistance in some of these riders and trackers, we are going to continue to have to file rate cases on a pretty repetitive basis. Our preference is not to have to file general rate cases to true-up individual items which are beyond our control like property taxes and transmission expense. If we are not able to achieve that in this case, that will be part of our discussion with the legislature, is that general rate cases that take 11 months and cause lag are not necessary or useful. And that will be our message and that message will be fresh because we just had a case that discussed it.

That's about all I could tell you at this point. Obviously, we need to finish the cases. We'll coordinate with our other utility companies in the state and we'll be working on a plan to talk to legislators about good, solid, practical solutions to cost recovery.

Paul Patterson - *Glenrock Associates - Analyst*

Okay, thanks for the clarity.

Operator

(Operator Instructions). And I'm showing no questions at this time. I would like to now turn the call back over to management for any further remarks.

Terry Bassham - *Great Plains Energy - Chairman, President, CEO*

Thank you, everybody, for joining us today. We will continue to keep you updated as we see results from the rate cases. And as always, feel free to contact our IR team with interim questions. Thank you much.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program. Everyone have a great day.

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