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EDITED TRANSCRIPT

IDA - Q2 2016 Idacorp Inc Earnings Call

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PRESENTATION

Operator

Welcome to IDACORP's second-quarter 2016 conference call. Today's call is being recorded and webcast live. A complete replay will be available from the end of the day for a period of 12 months on the Company's website at www.idacorpinc.com. (Operator Instructions). At this time, I would like to turn the call over to Justin Forsberg, Director of Investor Relations. Please go ahead, sir.

Justin Forsberg ***- IDACORP, Inc. - Director IR***

Thanks, Kaylee. We issued our earnings release and Form 10-Q before the markets opened today. Both are now posted at IDACORP website. The slides we'll be using to supplement today's call are also on our website. We'll refer to these slides as we present today's updates.

As shown on slide 2, on today's call we have Darrel Anderson, President and Chief Executive Officer, and Steve Keen, Senior Vice President, Chief Financial Officer and Treasurer, along with other individuals available to help answer your questions during the Q&A period.

As noted on slide 3, our presentation today will include forward-looking statements. While these forward-looking statements represent our current judgment or opinion of what the future holds, these statements are subject to risks and uncertainties that may cause actual results to differ materially from forward-looking statements made today. So we caution you against placing undue reliance on any forward-looking statements. The forward-looking statements listed on slide 3 are described in more detail in our filings with the Securities and Exchange Commission, which we encourage you to review.

On slide 4, we present our quarterly financial results. IDACORP's second-quarter 2016 earnings per diluted share were $1.12, a decrease of $0.19 per share from last year's second quarter. For the first six months of 2016, earnings per diluted share were $1.63, $0.15 less than the same period in 2015.

I will now turn the presentation over to Steve to discuss the results in greater detail and to review our 2016 key operating metrics.

Steve Keen ***- IDACORP, Inc. - SVP, CFO, Treasurer***

Thank you, Justin. And I want to take just a moment and thank a long-time voice that opened these calls, Larry Spencer, who's here with us today and who will be with us for a few more months. But Justin has now taken over as our lead introduction for this call, and I just want to acknowledge and welcome him to this process and thank Larry for his many, many years that he took care of us.

And with that, we had a good second quarter that exceeded our expectations, thanks in part to favorable weather during the last few days of June. Above-normal temperatures in the last week of June drove irrigation and air-conditioning loads higher than expected, but the second-quarter financial results were still less than the prior year. As a reminder, last year the Company recorded the highest second-quarter energy sales on record, as an early start to the irrigation season combined with a June heat wave in our service area to dramatically benefit sales in 2015. Looking ahead, our forward estimates include only normal weather expectations.

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On slide 5 you'll see a reconciliation of the change of net income from second quarter 2015 to second quarter 2016. Overall, net income was $9.9 million less than in the same period last year. Customer growth in our service area increased operating income by $2.7 million in the second quarter. However, decreased usage per customer lowered operating income by $9 million compared with the second quarter of 2015.

The application of the Idaho Fixed Cost Adjustment mechanism, or FCA, decreased revenues by $5.9 million in the second quarter and needs more explanation. Last year the Idaho Public Utilities Commission modified the FCA mechanism to use actual sales rather than weather-normalized sales. According to the Idaho Commission's order in the second quarter of last year, the change became effective January 1, 2015. The first-quarter impact of the change resulted in a $7.4 million positive income adjustment recorded in the second-quarter 2015 financial results. Comparing only the FCA impacts attributable to the second quarter 2015 to the FCA impacts in this year's second quarter, there would have been a $1.5 million increase in FCA revenues.

Other increases in operating revenue were primarily related to two factors. First, a $1.5 million revenue benefit in the second quarter of 2016 was due to higher average rates charged per kilowatt-hour based on levels of irrigation usage. The second factor was an approximately $2 million adjustment which lowered revenues in last year's second quarter per the methodology change ordered by the Idaho Commission regarding the power cost adjustment mechanism. Overall, Idaho Power's second-quarter operating income decreased $9.4 million year over year.

The decrease in income tax expense was largely a result of lower pre-tax income. Also, Idaho Power did not book any additional ADITC amortization this quarter, leaving $500,000 recorded for the six months ended June 30, 2016. Additional ADITC amortization is recorded based on the expected Idaho Power return on year-end equity in the Idaho jurisdictions. I will discuss this in greater detail in a moment.

Moving now to slide 6, we show IDACORP's operating cash flows for the first six months of 2016 and 2015, along with the liquidity positions as of June 30. Cash flow from operations for the first six months of 2016 was $137.9 million, a decrease of $33.1 million from the same period in 2015. This was primarily driven by timing of and decreases in working capital, lower net income, timing of distributions from an equity method investment, and changes in regulatory assets and liabilities.

IDACORP and Idaho Power currently have in place credit facilities of $100 million and $300 million, respectively, to meet short-term liquidity and operating requirements. The liquidity available under the credit facilities is shown on the bottom of slide 6. Although we do not plan to issue equity during the remainder of 2016, we are currently evaluating the renewal of our continuous equity program, which expired in May.

Turning to slide 7, with the exception of tightening the hydroelectric generation range, each of the financial and operating metrics listed on this slide remain the same, as presented on April 28, the date we reported first-quarter 2016 results. Through the first six months of this year, based on our estimate of return on year-end equity in the Idaho jurisdictions for 2016, we have recorded $500,000 of additional ADITC amortization. This is included in the income tax reconciliation table in Note 2 of the financial statements in the Form 10-Q filed earlier today. As of June 30, we estimated that Idaho Power will record approximately $1 million of additional ADITC amortization for the full year 2016.

I want to acknowledge that $1 million is at the low end of our stated zero to $5 million range, but with some below-normal temperatures in the early part of July and planning based on normal weather for the remainder of the year, the possibility of additional use of these credits still exists. With that said, our efforts have been targeted on preserving credits, and we will continue to be diligent in managing costs and growing revenues with the goal to preserve all credits for future years. I will add that this week's temperatures, at least in Boise, have returned to triple digits.

Finally, as discussed in the Liquidity and Capital Resources section of the Form 10-Q, the early redemption of first mortgage bonds due April 2019 resulted in Idaho Power paying a make-whole premium of $14 million to the holders of the bonds. The redeemed 10-year 6.15% bonds were replaced with 30-year 4.05% bonds, resulting in a significant improvement in both tenor and rate. The net tax benefit of the make-whole premium is $5.6 million, which was recorded in this year's second quarter. This benefit has been taken into consideration in reaffirming the earnings per share guidance range for 2016, along with our active management of costs.

I will now turn the presentation over to Darrel.

Darrel Anderson - ***IDACORP, Inc. - President, CEO***

Thanks, Steve, and good afternoon. As you have already heard and read, this quarter's results are fairly straightforward. We have continued to focus on Idaho Power's core business of providing reliable, responsible, fair-priced energy services.

We continued to see customer growth in the second quarter. Based on this and recognition of our service area in several publications and reports such as the one shown on slide 8, we continue our optimism about customer and economic growth prospects. We are seeing companies enter into and expand in various locations throughout the service area.

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One recent example is Great Western Malting, which is the oldest malting company in the western United States. Located in eastern Idaho, Great Western broke ground on a $75 million expansion to its existing malting plant last summer and is expected to be completed in 2017. Economic development officials in Pocatello say this expansion will have more than a $300 million economic impact on the region.

The organic nutrition company, Clif Bar, opened its 275,000-square-foot bakery in Twin Falls in late May of this year. Another production line at the plant is already in the works to go online in 2017.

As we have highlighted previously, southern Idaho has secured a record-setting seven major agricultural-related projects since 2012. According to a recent report by the Southern Idaho Economic Development Organization, these projects have generated 5,000 new direct and indirect jobs with a combined investment of over $770 million.

It is not just the agricultural sector that is driving growth. Recently, two California-based manufacturing companies elected to relocate to our service area, bringing with them over 100 new jobs.

For the 12 months ended June 30, 2016, Idaho Power's customer growth rate was 1.8%. Employment statistics remain strong. Preliminary data from the Idaho Department of Labor as of June 2016 shows unemployment in the service area was 3.9% compared to 4.9% nationally. Compared with last year's second quarter, employment in our service area increased approximately 2.3%, now exceeding 485,000 employed.

Also as of June 2016, Moody's Analytics forecasted growth in gross area product in our service area of 5.1% and 4.8% for 2016 and 2017, respectively. We have seen significant empirical evidence of robust growth in our service area in the last few years, and certainly during the last quarter, and we believe the growth prospects in our service area in the future remain positive.

Moving now to some of Idaho Power's 2016 initiatives, capital expenditures continue to be on target for the year. We expect an on-time and on-budget completion of the Selective Catalytic Reduction equipment, or SCRs, at Unit 4 of the Jim Bridger Plant in Wyoming during the fourth quarter. Additionally, there are two major upcoming milestones for the Boardman-to-Hemingway transmission line project. The Bureau of Land Management's schedule provides for the issuance of a Final Environmental Impact Statement in the third quarter of this year and a Record of Decision late this year. We recently kicked off our 2017 integrated resource planning process, which is our 20-year look at resources and demand, and expect to file this document next summer.

The Company continues to actively manage costs, targeting opportunities to optimize business practices for the benefit of our customers and our shareowners. We are focused on cost recovery and earning a reasonable return, as demonstrated by careful consideration of potential rate impacts and regulatory approvals related to Idaho Power joining the Western Energy Imbalance Market in 2018 and the timing of other large capital projects.

We continue to assess the need to file a general rate case in Idaho and Oregon in 2017 or 2018. As a reminder, our settlement stipulation that provides for amortization of additional ADITC and customer sharing is designed to continue beyond a potential general rate case in these years. The mechanism is in place through December 2019 or whenever we exhaust the $45 million of additional ADITC amortization available for use.

Turning now to slide 9, many of you know 2016 marks Idaho Power's 100th year of operations. In commemoration of the centennial, Chairman of the Board Robert Tinstman and I, as well as other members of the management team, have been invited to ring the closing bell at the New York Stock Exchange on August 1. It is certainly a fitting way to mark the principal contribution of IDACORP's and Idaho Power shareowners through the past century. We hope that you will view the closing bell ceremonies when the New York Stock Exchange closes this coming Monday afternoon.

Finally, looking forward to the rest of the year, slide 10 shows the projected August-to-October weather outlook. As you can tell from the map, the entire country is expected to see above-normal temperatures over the next three months. For the Idaho Power service area, current projections suggest there is at least a 50% chance of above-normal temperatures.

Regulatory mechanisms, such as the Fixed Cost Adjustment applicable to residential and small commercial customers and the annual power cost adjustment, mitigate the impacts of weather. As you are aware, these mechanisms allow us to share both the risks and the rewards of weather-related conditions with our customers.

Now Steve and I and others in the room today will be happy to answer any questions you may have.

QUESTION AND ANSWER

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Operator

Thank you. (Operator Instructions.) Brian Russo, Ladenburg Thalmann.

Brian Russo - ***Ladenburg Thalmann & Co. - Analyst***

I'm trying to get an understanding of under what scenario would you consider filing a rate case in Idaho, since you have a fairly unique rate structure which has worked well for you guys for the last few years?

Darrel Anderson - ***IDACORP, Inc. - President, CEO***

Brian, this is Darrel. One of the things that we will continue to look at is balancing how well we continue to manage our spend on the O&M side, how we continue to see customer growth that continues to come along, as we mentioned and I talked a fair amount about, as we're seeing a fair amount of growth. And so basically balancing those items and to determine whether or not, when we run the forecast, whether it's deemed necessary that we need to go in and ask for a change in price. So we'll continue to look at that. We'll look at our level of capital spend also. And it's a lot of those factors that we will consider in trying to determine when that is. And as I noted, right now we're looking, really, at into 2017, as at least the more likely period that we might consider filing.

But remember, our process takes seven months to happen. So it takes a little while to make anything happen. If we wanted something to go in as early as 2018, we would have to file something by June 1 of 2017. And so think about that timeframe. But right now, we're just continuing to evaluate and look at where our numbers line up.

Brian Russo - ***Ladenburg Thalmann & Co. - Analyst***

Got it. And do you have any idea of the scrubber-related O&M expense and depreciation expense might be?

Steve Keen - ***IDACORP, Inc. - SVP, CFO, Treasurer***

Brian, I don't think we have a number that we've published on those, but it's clear that that's one of the items, as Darrel mentioned, that we have to manage through, is that as we close more plants, we do pick up depreciation. And so the challenge for us is that the combination of what we get through the growth, new sales, and what we're able to manage just overall from the cost standpoint, those add up to offsetting the known cost increases, because there are some that come.

Brian Russo - ***Ladenburg Thalmann & Co. - Analyst***

Got it. And companies are starting to discuss pension expense in light of the lower interest rates. Any comment from you guys?

Steve Keen - ***IDACORP, Inc. - SVP, CFO, Treasurer***

I guess the one thing I would add is I think we're as -- like many, have thought eventually interest rates take some of that issue away. And if you'd asked me a week ago, I would have said, "Gee, I think interest rates are back to staying low for a long time," then Fed says what they said a day or so ago, and who knows?

But certainly, there's an element of it that if interest rates raise even modestly -- I'm talking 100 basis points -- you see a lot of the problem change. From our standpoint, we have a mechanism in place where we fund, basically, by cash. We are collecting some dollars from both Idaho and Oregon, but we don't have the income statement impact as much as we need to manage the cash impact. And so I think for us, it's maybe less of an issue. But we certainly have our eye on being able to earn adequate returns to match up with the growing obligation of the pension plan.

Certainly last year wasn't a huge return year, but if you go back, I think, over the last five years, we still are fairly close to the average earnings that we have to have in order to match up. So it isn't all doom and gloom, because we certainly have had a marginal return the last year or two, but we'll keep an eye on that. And we're putting money in annually. If you notice our discussions on that, we actually don't have -- our minimum funding requirement would be zero, but we are funding beyond that, partially to offset these kind of things and stay ahead of the game.

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Brian Russo - ***Ladenburg Thalmann & Co. - Analyst***

Got it. Thank you.

Operator

Paul Ridzon, KeyBanc.

Paul Ridzon - ***KeyBanc Capital Markets - Analyst***

You said that weather was hotter than normal. What was the impact of the FCA on the quarter?

Darrel Anderson - ***IDACORP, Inc. - President, CEO***

So the FCA was $1.5 million. Remember, in my script, if you listen to that when it comes back, quarter to quarter, FCA actually helped us slightly. Because remember, it's focused on certain parts of the equation and not all parts. So most of our lift, I would say, was irrigation related, and irrigation doesn't get moderated, helped or moderated, by the FCA. For the full month, I think our other revenues were actually down slightly. I think we said a $1.5 million benefit. So not a lot of impact, truthfully. I'd say the others were pretty close to normal.

Paul Ridzon - ***KeyBanc Capital Markets - Analyst***

And when you bring Jim Bridger SCR into service, will that go into rates, or do you have to do that through a GRC?

Steve Keen - ***IDACORP, Inc. - SVP, CFO, Treasurer***

We have to go through a GRC on that, Paul.

Paul Ridzon - ***KeyBanc Capital Markets - Analyst***

Okay. That's all my questions. Thank you.

Operator

Thank you. (Operator Instructions.) That concludes the question-and-answer session for today. Mr. Anderson, I will turn the conference back to you.

Darrel Anderson - ***IDACORP, Inc. - President, CEO***

Thank you, Kaylee, and thanks, all of you, for participating in our call this afternoon. We appreciate your continued interest in our Company and hope you have a great rest of the day. Thank you.

Operator

That concludes today's conference. Thank you for your participation.

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