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# EDITED TRANSCRIPT

DTE - Q1 2016 DTE Energy Co Earnings Call

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**Gerry Anderson** *DTE Energy - Chairman and CEO*  
**Peter Oleksiak** *DTE Energy - SVP and CFO*  
**Jerry Norcia** *DTE Energy - President and COO*

## CONFERENCE CALL PARTICIPANTS

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**Gregg Orrill** *Barclays Capital - Analyst*  
**Julien Dumoulin-Smith** *UBS - Analyst*  
**Shar Pourreza** *Guggenheim Partners - Analyst*  
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## PRESENTATION

### Operator

Good day and welcome to the DTE Energy first-quarter 2016 earnings release conference call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Barb Tuckfield. Please go ahead.

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### **Barb Tuckfield** - *DTE Energy - Director of IR*

Thank you, Cynthia, and good morning, everyone. Welcome to our 2016 first-quarter earnings call. Before we get started, I would like to remind you to read the Safe Harbor statement on page 2 of the presentation, including the reference to forward-looking statements.

Our presentation also includes references to operating earnings, which is a non-GAAP financial measure. Please refer to the reconciliation of GAAP reported earnings to operating earnings provided in the appendix of today's presentation.

With us today are Gerry Anderson, our Chairman and CEO; Peter Oleksiak, our Senior Vice President and CFO; and Jerry Norcia, our President and COO. We also have members of the management team to call on during the question-and-answer session.

I'll now turn it over to Gerry.

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### **Gerry Anderson** - *DTE Energy - Chairman and CEO*

Thank you, Barb, and thanks to all of you for joining us here this morning. I should take just a minute and recognize that this is Jerry Norcia's first time on this call as President and COO. Jerry was promoted into that position early in April.

I think many of you know Jerry or have met him on visits, but Jerry, just a brief history, came in as president of our gas storage and pipelines business and really helped to build that business. Then took over as president of our gas utility, along with his role at GSP. Most recently was president of our electric operations, and then as I mentioned, moved into his role as President and COO just about a month ago.



Well, I am going to start the discussion today with an overview of our results in the first quarter as well as a number of key developments at the Company. Then I'll turn things over to Peter to give you a financial update, and then we will wrap up and take your questions.

So moving on to slide 5, we continue to make good progress on a number of fronts. With one quarter behind us in 2016, I feel very good about our year-to-date financial results and our ability to deliver or exceed our full-year guidance.

Energy legislation continues to move forward in Lansing. In fact, this is a key week, as it turns out and I will describe that in a minute. And our NEXUS gas pipeline project continued to move forward toward its 2017 in-service date, and I will give you an update on progress on that front in a few minutes as well.

So concerning our financial performance, moving on to slide 6. As I mentioned, we are off to a very good start. We delivered first-quarter operating earnings of \$1.52, which I feel great about relative to our plan for the year.

We came into 2016 expecting a warm winter. We were talking about that prior to the call. We started last July planning for El Nino, so we came into the year with a plan expecting a standard deviation or more warmer this winter. And it came, but we came out of the first quarter in great shape. So that all worked out fine.

And given that, we are on track to deliver our earnings guidance and another year of earnings growth. And assuming that we do that, 2016 will be our 10th consecutive year of meeting or beating our earnings targets.

As you know, we've also been growing our dividend in parallel with earnings and we have every intention to continue that. And our balance sheet continues to be in great shape. In fact, Fitch, back in February, upgraded us. So bottom line, as we head into the second quarter, I feel great about our financial position.

Moving on to slide 7, as I said earlier, energy legislation continues to progress in Lansing. The current regulatory construct in Michigan was established by legislation passed back in 2008 and the key provisions of that legislation and our current construct are laid out at the top of the slide. Those provisions have and continue to serve the state of Michigan very well.

But in preparation for a significant investment in new-generation assets in our state as we retire older assets, we've been working on an update to the 2008 legislation over the past year. And this week, Senator Mike Nofs, who is Chairman of the Senate Energy and Technology Committee, will introduce his substitute bills and take testimony from a range of key stakeholders. In fact, I'm going to be up in Lansing on Thursday testifying.

The legislation that Senator Nofs has fashioned has a number of key features. So it establishes firm capacity requirements for all electricity providers in Michigan. But in particular, establishes requirements for the first time for the retail open access suppliers or choice suppliers.

That's a key reliability provision as the state moves into retiring and rebuilding generation. That 10% of the market needs to be planned for and that's what the legislation is targeting.

The legislation also sets up an IRP, or integrated resource planning, process that will enable long-term resource planning and will establish a process for investment preapproval. And then finally, the legislation establishes incentives for energy efficiency investment and it enables decoupling related to energy efficiency and makes it possible for utilities to apply for broader decoupling to the Public Service Commission as well.

So Senator Nofs expects to work these bills hard this week and the following week and then we'll move them out of committee for a vote on the Senate floor when he feels the time is right for that. And then we expect that this legislation will become -- will move over to the House and become the basis for discussions and action there.

So we also continue to make progress on our NEXUS pipeline project and slide 8 provides a summary update of that activity. As the left-hand side of the slide shows, NEXUS originates in arguably the best dry gas geology in the country, in the Utica shale. And it then runs north and west across northern Ohio, where there are numerous opportunities to interconnect with LDC power plant and industrial loads.



And then the pipe heads north to interconnect with the Vector pipeline in Michigan, which ties into a very large gas storage complex in Michigan and in Ontario. And Vector also enables it to serve LDCs in Ontario, Michigan, Illinois, Wisconsin, and other Midwest states. The NEXUS remains on track to be placed in service in the fourth quarter of 2017. A couple of noteworthy first-quarter accomplishments for NEXUS are listed on the right-hand side of the slide.

As I mentioned, the pipe runs across northern Ohio, and during the first quarter, we increased our interconnect agreements along that stretch from 1.4 BCF per day to 1.75 BCF per day. And these interconnect agreements represent great future market opportunities for NEXUS, which is a 1.5 BCF designed pipe.

We also ordered compressors for the pipe in the first quarter. So both the steel, the pipe, and the compression for the project are on order. And finally, we continue to advance our work with the FERC and that's going well. And we continue to expect our FERC notice of schedule here during the second quarter.

So before I hand things over to Peter for a financial update, I want to summarize on slide 9. We have for years talked to investors about delivering 5% to 6% annual earnings-per-share growth with high reliability and consistency and pairing that with healthy dividend growth.

And on the right-hand side of the slide in the ovals, you can see that our actual EPS growth in recent years has been 6.5%, and we have grown the dividend at just above 5.5%. And given our start to 2016 in the first quarter, as I said earlier, I feel really good about our ability to continue that pattern over the course of this year.

So with that said, Peter, over to you.

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**Peter Oleksiak** - DTE Energy - SVP and CFO

Thanks, Gerry, and good morning to everyone. I'd just start on slide 11. And as Gerry mentioned, DTE Energy's operating earnings for the first quarter were \$1.52 per share. And for reference, reported earnings were \$1.37 per share. For a detailed breakdown of EPS by segment, including a reconciliation to GAAP reported earnings, please refer to slide 29 of the appendix.

This slide shows our quarter-over-quarter operating earnings by segment. We'll start at the top of the page with our two utilities. It's important to remember that the first quarter last year was one of the coldest on record. In fact, February of 2015 was the coldest February in the last 50 years. The first quarter of 2016 was actually one of the warmest on record.

So primarily driven by weather, earnings for both electric and gas utilities were down quarter over quarter. DTE Electric's earnings were \$127 million for the first quarter this year compared to \$136 million last year. Along with weather, DTE Electric's earnings were lower due to the absence of the revenue decoupling mechanism amortization in 2016.

This revenue decoupling amortization was part of our strategy that extended the time frame in between rate cases by four years. The amortization was offset by the implementation of new rates last July. A further breakdown of DTE Electric's quarter-over-quarter results can be found in the appendix on slide 21.

For DTE Gas, earnings for the quarter were \$87 million compared to \$111 million last year. As stated earlier, the significant change in weather was the primary driver of this variance.

Gas storage and pipeline earnings were \$30 million for the quarter. Earnings for the quarter were up \$3 million over last year due to higher pipeline and gathering earnings from production that came online after the first quarter of 2015. Storage earnings were also higher than last year due to lower maintenance expenses.



Moving down the slide, earnings for our power and industrial projects were \$21 million for the quarter, down \$12 million from the first quarter last year. This decrease was primarily driven by lower earnings in the steel sector. There is seasonal variability related to the REF volumes, and for the balance of the year, the REF will help offset the steel sector decline.

Earnings for corporate and other were negative \$7 million for the first quarter of 2016. \$18 million favorable over last year due to a first-quarter 2015 effective tax rate adjustment, which unwound during the rest of that year. So earnings for our growth segments for the first quarter were \$258 million or \$1.43 per share compared to \$282 million or \$1.58 per share last year.

To round out our operating earnings, we include the results of our energy trading business. At energy trading, the first-quarter operating earnings were \$16 million, up \$4 million from the first quarter last year, driven by stronger realized gas portfolio performance.

Our trading company is off to another good start. Trading's economic contribution for the first quarter 2016 was \$18 million. Slide 28 of the appendix contains our standard energy trading reconciliation, showing both economic and accounting performance. We typically wait until the midyear earnings call to assess the trading company's range of accounting income contribution for the year. At that point, we have a good sense of how much accounting income will be flowing through to cover current-year operating expenses.

I'd like to move now to slide 12. Slide 12 provides a quick overview of our capital expenditures through the first quarter of the year. Capital spending was lower than last year, primarily due to the purchasing of a peaking generating asset in 2015.

Our CapEx guidance range remains at \$2.5 billion to \$2.7 billion for 2016. I'll go into more detail on some of our utility capital plans on the next two slides. I'd just like to turn now to slide 13 and our electric utility.

I want to highlight one of the key areas of focus for our electric utility segment, which is improving customer-related distribution reliability. We are making significant investments in our distribution infrastructure to improve reliability and address growth in certain areas of our service territory.

Over the next 10 years, we'll spend \$6.5 billion replacing aging infrastructure and overloaded substations as well as consolidating existing substations and adding technology and automation to provide greater visibility into the system for outage prevention and detection. As we said in the past, this 10-year investment of \$6.5 billion of distribution infrastructure can increase up to an additional \$4 billion of reliability investments. Customer affordability is at the forefront of our planning and will guide and determine how much total distribution reliability investment we will do in this time frame.

Now on slide 14, this slide highlights a large component of our investment at DTE Gas expanded main renewal program. We'll invest \$600 million over the next five years upgrading the gas system. Our plan to replace 4,000 miles of cast iron and unprotected main steel was accelerated to cut the completion time in half from 50 years to 25 years.

The MPSC approved the acceleration of the infrastructure recovery mechanism at the end of last year. Upgrading the gas main system benefits our customers by reducing costly leaks and assuring the basic gas infrastructure in our service territory is there for future generations. As you can see from the previous two slides, our CapEx plan will address the needs of our customers and the aging infrastructure while being mindful of customer affordability.

We've been consistent in our messaging over the years that maintaining a strong balance sheet is priority. So on slide 15 provides the key balance sheet metrics we target and monitor: FFO to debt and leverage. This slide shows the projected level for each metric.

Our near-term equity issuance plans are \$200 million to \$300 million over the next three years and we continue to evaluate our equity needs for this year. As we discussed on our year-end call, extension of bonus depreciation provides \$300 million to \$400 million of favorable cash flow over the next five years, which help reduce our equity needs in the near term. The strength of our balance sheet sets us up nicely as we enter a period of incremental infrastructure improvement and we are confident that our plans allow us to maintain this balance sheet strength.



Let me wrap up on slide 17, then we can move to Q&A. With a strong first quarter, even with a good amount of unfavorable weather, we are confident that we will achieve our operating earnings guidance of \$4.80 to \$5.05 per share, which will extend our streak to 10 consecutive years of meeting or exceeding our initial EPS guidance.

We are making significant utility infrastructure improvements that will continue to provide affordable and reliable service to our customers. We have meaningful investment opportunities at our gas pipeline segment with our investments in Millennium, Bluestone, and the NEXUS pipeline. In our power and industrial segment, we have opportunities with building on-site cogeneration projects.

Going forward, we continue to target operating EPS of 5% to 6% for our growth segments. And part of our shareholder value equation is to continue to grow our dividends in line with these earnings. We maintain our commitment to a strong balance sheet, which can provide future growth opportunities.

Before I open up to Q&A, I know many of you on the call have been waiting for my Detroit Tiger update, so I'd like to give a quick update on my hometown Detroit Tigers because no DTE earnings call would be complete without it.

This year definitely started out well for the Tigers, but recently, they've been having some problems with their pitching. The weather for this year's home opener game in Detroit was definitely favorable to our gas utility, as it was one of the coldest home openers ever played in Comerica Park. Our fans braved the weather and packed Comerica Park to watch us beat the Yankees, which was our eighth consecutive home opening win. It's always a good day when we beat the Yankees.

With that, I'd like to thank everyone for joining us this morning. So Cynthia, we can open up the lines for questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Jonathan Arnold, Deutsche Bank.

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### Jonathan Arnold - Deutsche Bank - Analyst

Couple of quick questions. I think I understood that the delta in the tax rate on the quarter was primarily due to a higher-than-normal rate in Q1 last year. But I'm just curious if the 26% that we see on the GAAP income statement is what you consider to be normal here or whether there was also a benefit in Q1 kind of versus the run rate.

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### Gerry Anderson - DTE Energy - Chairman and CEO

No, it is normal and our effective tax rate is close to that 26%. It will time out throughout the year. Last year, just because of reported earnings being higher, we had higher tax expense that quarter, which normalized throughout that year.

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### Jonathan Arnold - Deutsche Bank - Analyst

Great, okay. And then I was just curious -- Gerry, in your opening remarks, you talked about having prepped for the El Nino winter and come out of it (technical difficulty). You obviously had a big quarter in the trading business.

I'm wondering if -- was that part of the positioning for the winter? You set yourselves up there, or was it expense management? Just give us a little more flavor of what you were alluding to terms of the offset.



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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

When I said we came out of the quarter the way we wanted, I was really talking about our growth segments. The trading I would -- it's really separate discussions. So no, we weren't talking about positioning our trading company.

What we really did is just look at the odds the way the El Nino was setting up last summer that we would have a warm winter. And the odds are very high when you look across past statistical data. So we all looked at ourselves and said look, if the odds are this high, we are just going to take it as a given and plan for it.

So we did go into our expenses. We went after additional productivity in the business. So we always look for productivity improvements, but we went for more than normal. That was hard work to put the plan together, but it paid off.

And we don't publish our plan and make public our plan, but I do feel really good about the way we exited the quarter in our growth businesses relative to the plan we had for the year. And that's why you are hearing a confident tone on our ability to play out and meet or exceed our guidance for the year.

Trading -- just to comment on that, they had a really good first quarter. As Peter said, we usually wait until midyear to kind of give you a better sense. So we'll probably on our midyear call update you on those earnings and then give you probably conservative forecast for where we think trading will land for the year.

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**Jonathan Arnold** - *Deutsche Bank - Analyst*

Can you give any insight into how -- what was the main driver of their performance in a risk context, perhaps?

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

We've been migrating that business more and more physical. So for example, the gas business is a very active business and moving gas both in the Marcellus and beginning to play in the Utica area to take gas to market. So that's been a growing and profitable segment.

We also are a supplier to other utilities and some of their full requirements services businesses. And that segment did very well for us this quarter. So it's kind of lining up supply for other utilities who are, you know, in markets that have restructured, but still have a responsibility to supply their retail customers. We provide them wholesale to do that.

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**Jonathan Arnold** - *Deutsche Bank - Analyst*

Great. Thank you very much, guys.

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**Operator**

(Operator Instructions) Gregg Orrill, Barclays.

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**Gregg Orrill** - *Barclays Capital - Analyst*

Could you talk a little bit more about the legislation and your thoughts around the prospects there and the timeline?



**Gerry Anderson** - *DTE Energy - Chairman and CEO*

I've been saying for awhile that Mike Nofs is a good guy to be steering this. Mike was one of two principal architects of the 2008 legislation, so he is the most knowledgeable guy in the Michigan legislature on this whole topic.

Mike has been working this in a very systematic way since early this year, and he's now moved it to a point where he feels like he's ready to take the bills -- there are two bills -- out into the open and take commentary this week and next. And he'll then evaluate, look, do I feel like things are right for a vote.

I think his intention is to come through that discussion period and bring it to a vote here sometime in May; probably the first half of May ideally. And then we'll -- that legislation will be pushed back over to the House. Then the question in the House is how quickly can it move there? Will they be in a position to move it before the summer recess? Or like in 2008, will it come back after the summer recess and be acted on then?

In 2008, just having been part of that, I spent kind of a year of my life involved in that one. The way it played out is actually in that case, the House finished action just prior to the summer recess, and then the Senate came back and acted right after the recess. So we'll wait and see, but I think the hope would be that we would get out of the Senate and act on it in the House as well prior to the recess. But if that didn't happen, it could play out like 2008 did.

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**Gregg Orrill** - *Barclays Capital - Analyst*

Okay. Thanks.

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**Operator**

Julien Dumoulin-Smith, UBS.

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**Julien Dumoulin-Smith** - *UBS - Analyst*

So just coming back to the NEXUS project -- don't want to belabor this one too much this go-around. But just curious a little bit on the nature of the contracts signed, and specifically, if you could elaborate on future opportunities for further contracts, whether they are generators or utilities.

And then ultimately, as you think about moving forward on the project, where do you stand under contracts today from an ROE perspective on the project? Taking it as a given that you are going to move forward, how does it compare versus what you are targeting ultimately in terms of the ROE range you've kind of alluded to?

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

I think I'm going to turn this one over to Jerry Norcia. So Jerry, why don't you respond to those?

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**Jerry Norcia** - *DTE Energy - President and COO*

Great. So the nature of the contracts we have on NEXUS today, about half the capacity is committed to buy LDCs in Michigan as well as Ontario. And then we have three producers that are also anchor tenants. So I would say about half is LDCs and half is producers.

In terms of incremental markets, I think it will come from both classes of customers. We are pursuing both LDCs in Ohio, Michigan, Ontario, and the Midwest for incremental volumes, as well as other producers that are interested in moving gas to these markets. I think we are well positioned for that. So those discussions are underway.



In terms of returns, we are happy to proceed with the returns that we have based on the contractual commitments that we have today. And as we've said before, I think we've got about two-thirds of our total commitments signed with long-term contracts today.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

Just to add onto that, I think we've said in discussions with investors previously, we typically move ahead of these projects at about 80% subscription level. We are a bit below that, obviously, because the market took a pause while we were in process.

But the combination of the geology here and those interconnect agreements, those 1.75 BCF of interconnect agreements, which really aren't a substantial part of our subscriptions right now, I mean that represents more capacity than the pipe itself has. So we think that will be a significant source of future demand, not to mention markets in Illinois, Wisconsin, etc. So the combination of the quality of the geology and so forth is what's given us the confidence to move forward.

I would say that you really create the hot value out of pipeline projects as you get full subscription and then expand. So I would say we are kind of down in the willing to proceed, but not in the hot zone with the level that we are at. So we are looking to add capacity over time. And demand --

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**Julien Dumoulin-Smith** - *UBS - Analyst*

Got it. But it wouldn't -- I'm sorry, go for it.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

No, I said add capacity. I really meant add new customers over time to first fill and then expand.

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**Julien Dumoulin-Smith** - *UBS - Analyst*

Got it, all right. But no specific ROE expectations given the two-thirds, though?

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

I would just characterize it as kind of meeting our threshold requirements. But we're looking to move it from meeting our kind of threshold requirements to taking it up to what really makes a pipeline project sing, which is getting into the full and then expansion zone. So we are happy to proceed, given where we stand now.

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**Julien Dumoulin-Smith** - *UBS - Analyst*

Got it. And then if I can ask you to elaborate a little bit on the P&I side of the equation. You commented on softness in the first quarter and specifically comment that REF would help offset it through the balance of the year. Can you elaborate a little bit more on specifically how the numbers are turning out?

And then with regards to the P&I more broadly, how are you thinking about this business and the optimization of the overall portfolio of businesses you have in the context of [the slide]?

**Peter Oleksiak** - DTE Energy - SVP and CFO

We anticipated the softness in the steel sector, so we put that into our guidance. So as you look at the first-quarter results, that was anticipated when we published the guidance for the year.

For the REF segment, that's tied to coal production. There is seasonality. You know, most of the coal production occurs in the third quarter. So we'll see those REF earnings helping to offset the steel sector. We also had some projects come in late last year on the REF segment. So you'll start seeing those materialize as well coming into at the second half of this year as well.

So there is seasonality with the REF we do. And we overall are confident with the segment guidance that we put out there for P&I.

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**Julien Dumoulin-Smith** - UBS - Analyst

And with regards to the future P&I?

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**Gerry Anderson** - DTE Energy - Chairman and CEO

I think on the future, a couple thoughts. So REF will continue to be a good business and source of cash flow. Steel is one of those things where we've been through this before, so we contract with our steel customers. But contracts rollover and we had one of the contracts rollover at a soft point in the steel cycle.

But our typical experience is a couple years after the soft point, you are often in a point of recovery. And not long after that, a hot point in the steel market. So I think will have the opportunity to see that part of the P&I business return. That's certainly been our experience over the years in past ups and downs in steel.

The most active area for investment, I think Peter mentioned, is cogeneration projects. We have a number of those that are under serious discussion with counterparties. So we would expect that to be the place where we could put quality capital to work.

And we continue to be focused, as we kind of laid out in our five-year plan, on understanding that the REF earnings roll off in the early 2020s, that we would backfill those earnings with quality investments like the cogeneration. And that's the plan for the Company in terms of producing the 5% to 6% earnings through 2020 and beyond.

So we've got a 10-year plan. We are counting on P&I growing in absolute terms, kind of holding its own as REF rolls out while the other segments continue to grow.

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**Julien Dumoulin-Smith** - UBS - Analyst

Got it. But net-net for this year, kind of flattish as one-offs [get together].

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**Gerry Anderson** - DTE Energy - Chairman and CEO

Yes, I think that's right. We are still feeling flattish. As Peter said, steel was known and we knew that last September when we had analysts into Detroit. But REF is both cyclical and was a bit soft in the first quarter, just because of a warm winter and substitution of gas for coal and those sorts of things.

So it was down somewhat. But as we assess the prospects for the balance of the year, we still feel good about the guidance we have out there for the segment.



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**Operator**

Shar Pourreza, Guggenheim Partners.

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**Shar Pourreza** - *Guggenheim Partners - Analyst*

Could we just get a quick update on Bluestone and then sort of if you could just elaborate on any contingencies you have in place? If sort of that production schedule with the producers remains kind of weak?

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

Go ahead, Jerry.

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**Jerry Norcia** - *DTE Energy - President and COO*

Yes, I think right now, we are feeling very good about the guidance we issued for the midstream segment. Production that's flowing is in line with what we had estimated. And actually, we also feel good about the future there.

I think the prospect for Southwestern drilling in that area as commodity prices continue to strengthen become more positive as time goes on. So we feel real good about where we are in 2016.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

Yes. Southwestern was out publicly talking recently. And I would say that what we are seeing in our exposure to Southwestern is a very consistent with their comments publicly and consistent with the plan that we have out. So when Jerry says we feel good, I think we would say that it's consistent with what we expected and is playing out in a way that supports the plan.

And then you look down the road, you are beginning to see gas prices for early next year strengthen. And I think they were \$3-ish when we were talking about them yesterday. And you know, people keep concluding that -- so drilling has pulled back, but gas declines to 15% in the United States. And you can only allow a 15% decline before -- only allow that for so long before you need to begin to backfill it.

And the most obvious places for Southwestern and other people to begin drilling again is in the Northeast Marcellus and in the Utica. I think the well quality there is still high. So our expectation is we pushed up gas supplies in the country awfully hard in 2015. People are on a pause, but they are going to need to step back into it. And when they do, we expect it to be in the areas we have exposure to.

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**Shar Pourreza** - *Guggenheim Partners - Analyst*

Got it, that's helpful. And then could you just maybe elaborate on where you are at as far as any potential midstream acquisitions to fill any gaps? Or are we still kind of far off?

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**Peter Oleksiak** - *DTE Energy - SVP and CFO*

We've been in the process of looking at many assets, or at least a handful, that we were very interested in. One of the things that we are finding is that these assets are still trading at premium values. Some recent transactions have illustrated that. We are -- we still have a handful that we are looking at and actively pursuing.

I think in addition to that, we are also looking at greenfield opportunities, where we've had most of our success in the last 12 or 14 years in this space. So we've got both in motion to secure incremental growth for this business.

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**Shar Pourreza** - *Guggenheim Partners - Analyst*

Okay, got it. And just lastly on your capital outlook, obviously you guys have more capital than you can afford. And I think historically, sort of the rate impact to the customer has been that [sea link]. What -- is there any sort of guidance you could provide as far as what rate inflation you target when it comes to your spending outlook?

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

You know, if you look at our recent performance there, rates have been negative. So you go back to 2012 and compare them to today, we are down. And even after the current rate case plays out, we'll be flat to down to 2012. So we've been able to work our way through a very heavy capital investment period with rates down. And I'm talking about base rates.

The future -- we've consistently said that we are trying to keep rate increases in the range of inflation. So around 3% as you work your way through one of these intense capital investment cycles. And that's going to require us to both measure the pace of capital investment, but also keep the focus on productivity and continuous improvement that we've had in order to do that.

So you know what the blend of capital and O&M is. We got to keep the O&M. Our O&M in recent years, the increase has been zero. And when you can blend a zero with the increases that come from capital, you can hold it to something reasonable.

Now, we can't commit to zero in the future. We worked in the past very, very hard to keep it there. The future, you know, is -- that's unlikely. You can't continue that forever. But we will work hard on C&I and we will continue to measure the pace of investment.

But I think we've said that, for example on our distribution business, there's a lot of demand for investment. So we are going to have to high grade those projects and do the most important ones. And we're really doing that from a customer affordability perspective.

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**Shar Pourreza** - *Guggenheim Partners - Analyst*

Terrific. Thanks so much.

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**Operator**

Greg Gordon, Evercore ISI.

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**Greg Gordon** - *Evercore ISI - Analyst*

I think you gave us a good framework for how you're thinking about power and industrials in terms of what you have to achieve to hit your guidance. But frankly, I think the stock is -- has underperformed year to date. Not because people are worried about your utility businesses, but because they are worried about that business and they are worried about the gas pipeline and storage business. And the hurdles to hit the guidance you've laid out.

So focusing back on the pipeline business, NEXUS is two-thirds contracted, but these interconnect agreements are pretty substantial. Should we assume that shorter hauls for those interconnects at a certain percentage of those interconnect commitments could get you well into the range of an acceptable ROE on the pipe? Or do you need to get fully contracted for delivery to dawn at a higher percentage in order to hit your return hurdles or some combination of both?



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**Jerry Norcia** - *DTE Energy - President and COO*

I think both will happen. So I think what interconnect -- these interconnect agreements that we have really provide the pipeline with a lot of diversity of supply opportunities. So our shippers, long-term shippers on the pipe as well as new shippers that we expect to come on the pipe will use these interconnects as ways to deliver the various pipeline -- various markets up and down the pipe, especially in Ohio.

And the way I expect that those will turn into real opportunities and real commitments -- absolutely. I think that's a given that that will happen. I think in terms of more long haul, we are in discussions with several parties to sign them for more long haul.

So I think what you'll see here as the pipeline builds, you'll start to see those interconnects become very active market points for us and provide the what I would call a lot of optionality to future shippers on the pipe. And I think that will make it a very attractive pipeline that will allow us to get both short-haul and long-haul commitments. So I expect both to happen.

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**Greg Gordon** - *Evercore ISI - Analyst*

Okay. In terms of permitting, we just saw obviously a big negative surprise out of New York last week on a different pipeline project. What are the remaining permits you need, beyond just the FERC approval, to get this pipe into the ground?

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**Jerry Norcia** - *DTE Energy - President and COO*

I think the big one we are waiting for right now is the FERC notice of schedule, which we expect to happen here in the second quarter. And I think we are in really good shape with that. We are getting very good feedback from the FERC in terms of the quality of our filings.

I think a lot of our issues we are managing quite well -- routing issues. We are well underway with our right-of-way acquisition process. And I think in terms of other permits, there are some large customary permits that come with a FERC-regulated pipeline, like the US Army Corps of Engineers and other various permits.

But those are the big ones. I think the FERC order, which we expect by the end of this year, and also the other large customary permits. I think they are proceeding very well at this point in time.

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**Greg Gordon** - *Evercore ISI - Analyst*

Okay. And then when I look at -- go back and look at your year-end analyst deck, you said you -- your aspiration is to grow operating earnings from \$110 million at the midpoint in 2016 from this segment to \$170 million in 2020.

If Bluestone were to sort of flatline from here in terms of its earnings contribution and you didn't achieve any bolt-on acquisition, what would that number be? Would it be significantly lower? Would it be only modestly lower? Because really, just the crux of the issue on people's problem with valuing the stock is concerns over the growth in this business.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

Yes. So I'd say the prospects of Bluestone flatlining are -- I wouldn't frame it that way. We are expanding Bluestone and we are expanding Millennium. I think the prospects we see are for more of that.

So there is a -- you were mentioning a cancellation of a pipeline. What we are seeing in the Northeast is a continued pull for gas. They have to have gas for power generation and the oil-to-gas conversions continue. So the demand for gas continues to be very, very strong, but there's real resistance

in New York and in other areas of the Northeast to new pipeline. And I think that's what that's likely to do. In fact, New York called this out explicitly is bias toward expansions of existing pipes.

So I think the likelihood of some of this resistance you are seeing is that owners of existing position, including Millennium and Bluestone, will see people coming to them as the most credible and doable paths and expansion paths to market. So I would just start by saying that I think what we are seeing evolving in the market is a positive for the asset position we have there.

Bluestone and Millennium are attached to really good geology. And there is resistance in the market to creating new outlets, altogether new outlets, for that geology, which means the existing ones are going to have to expand.

And then the long-term growth -- NEXUS is an important part of that growth. But when we look out five years and ask what is the current dynamic in 2016 really mean for 2020? Not much. The gas demand in 2020 is going to be what it's going to be. And power generation conversions are going to be underway. And so the geology is going to have to deliver it. The pipes are going to have to deliver it.

Now, I think that you can say in the short term did production get out in front of itself a bit with a lot of excitement in the market? The answer to that is obviously yes. So there is an adjustment in the near term and, you know, a -- it's changed the past to get to 2020, but the ultimate point that the market needs to achieve in 2020 hasn't changed for either production or delivery through pipes to meet demand. So we really don't see a lot of impact long term, although the path to get there has changed from what it might have been.

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**Greg Gordon** - *Evercore ISI - Analyst*

Okay. Thanks a lot, guys. Have a good day.

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**Operator**

Paul Ridzon, KeyBanc.

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

So with Senator Nofs prepared to move the bill this week, what do we read into that as far as any progress that may have been made with the schools and with the Chamber of Commerce?

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

So Senator Nofs has been in active discussion with the Chamber. And I think I will -- I'm not going to put words in the Senator's mouth on the coalition he's put together. I think it would be better for him to play that out. But he has been in active discussion with the Chamber.

I think he's also put some provisions in the bill that broaden its interest to his Democratic colleagues. So if you look at the energy efficiency provisions, that's positive in terms of broadening the appeal.

He also does have the 30% goal. It's not a mandate, but it's a goal by 2025 for renewables and energy efficiency. That's something the administration has advocated for, as have Democrats in the House. So I do think what you see is Senator Nofs listening very, very carefully to a whole range of participants trying to broaden the coalition to a point that he could be successful.

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

And it's my understanding that the bill, when we see it, will have a provision where shoppers who leave actually have the opportunity to come back. How are you thinking about that?

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**Gerry Anderson** - DTE Energy - Chairman and CEO

Right. So they do today and they will in the future. We never thought there would be or should be a prohibition of retail open access customers coming back. But the -- I think what you'll see when you look at the legislation is that there's a lot more integrity now in terms of the reliability provisions related to this.

So suppliers to the retail open access market need to carry their fair share of local resources. That needs to be real. Need to have ties to real local resources for reliability. Customers who leave the queue, if somebody should come out from under the cap and somebody goes in, will be paying a demand charge. So there's a series of provisions, without me going into all the details, that really do shore up the reliability for that -- the reliability provisions related to that 10% of the market.

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

Thank you very much.

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**Operator**

Andrew Weisel, Macquarie Capital.

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**Andrew Weisel** - Macquarie Capital Securities - Analyst

Quick question first on the distribution reliability. You are showing the \$6.5 billion 10-year plan here. You've previously talked about potential for that to be over \$10 billion even.

Remind us: is that give it potential to add some of the extra stuff there? Does that depend on your ability to cut costs or the state energy law? Or what might be some of the swing factors of getting that into the plan? And when might those decisions be made?

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**Gerry Anderson** - DTE Energy - Chairman and CEO

So I think what we've said on that one is there's a lot of demand on our distribution system. It's an aging infrastructure system. As we evaluate the need, the need currently outstrips what we think customer affordability will enable.

So in order for us to do more of that and to kind of work our way into that backlog, it would depend on us finding productivity opportunities. Or if there were things, for example, that evolved on the generation side that were -- required less capital, we could conceivably push some of this needed investment in.

But we are kind of calibrating how much of that we do based upon affordability. Because we've consistently said that companies that don't pay careful attention to that when they are going through a big investment cycle end up losing. You just need to go through these cycles in a way where your customers feel their affordability is workable.

So that's really what determines how much of the \$10.5 billion we would spend versus the \$6.5 billion. And you are right: if we can find either capital offsets or productivity offsets, those are the things that would enable us to do more of that needed investment.

**Andrew Weisel** - *Macquarie Capital Securities - Analyst*

Okay, great. Next question is related to Millennium in New York. It's something I already made reference to the -- a different pipeline basically getting shut down because of it because of regulators not supporting pipeline expansion there. Do you see any risk to the plans for Millennium specifically?

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**Jerry Norcia** - *DTE Energy - President and COO*

The way I'll answer that is that with our pipeline investments that we've been able to secure through the FERC as well as with New York regulators, for example, we've been able to secure an expansion of Bluestone most recently through the New York regulators. And that's actually a pipeline regulated by New York, in New York. And then secondly, we secured the last two compressor expansions for Millennium through FERC as well as working with New York regulators.

So I think what we are -- as Gerry described earlier, you know, I think the regulators are pointing towards existing assets as ways to expand into a growing market. So, as you know, we've got a pipeline expansion where we've made a FERC refiling and that's going well. We are in active conversations with regulators in Albany on that expansion and we feel that those conversations are going well. So at this point, we feel pretty confident that we will secure our expansion approvals for Millennium.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

Bluestone runs both in Pennsylvania and New York, so you need approvals out of both states. But our recent expansion of Bluestone -- the conversations were very productive. And as Jerry mentioned, same was true for Millennium.

So our experience has been that when the need is clear and you are dealing with an existing asset with I guess you would say more modest implications, you can have a productive conversation and work your way through it. And that's what our last two rounds of discussion in Albany have produced.

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**Andrew Weisel** - *Macquarie Capital Securities - Analyst*

Very good. Last question. You added a comment there about continuing to evaluate current-year equity needs. You previously talked about targeting \$100 million of equity in 2016.

Which direction are you thinking? Are you trying to find ways to maybe reduce that number? Or is that more an implication that if you were to make an acquisition, for example in the midstream business, maybe you would issue some equity?

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**Peter Oleksiak** - *DTE Energy - SVP and CFO*

We always go into the year -- we have a big focus on cash in the Company. So we did indicate that over the three-year period is \$200 million to \$300 million. And then we potentially can do up to \$100 million this year.

So we are assessing that. Our goal would be if we can to make that zero. It's probably too early to say that. We're going to have to see how the year plays out and the cash flow of the Company plays out. I'll still say the \$200 million to \$300 million over the three-year period is still a good number. And we are assessing how much do we actually need to do of that \$200 million to \$300 million this year.

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**Andrew Weisel** - *Macquarie Capital Securities - Analyst*

So it's more a timing?

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**Peter Oleksiak** - *DTE Energy - SVP and CFO*

Yes.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

I'd say I think what Peter is indicating is that I think our Q says up to \$100 million, which implies that the bias would be down, given everything we know. But your comment was also right. If we found a great opportunity for investment that we thought created a lot of value, that could be the thing that pushes you up toward the high end of equity. So those are really the two balances.

As Peter said, we are always working cash and cash flow and we are off to a good start. So our hope would be to be playing out in the up-to zone, not the add \$100 million. And the one potential offset is if we found a great investment.

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**Andrew Weisel** - *Macquarie Capital Securities - Analyst*

Will the equity needs have an impact on the dividend decision, which you typically announce in June, and have a relatively low payout ratio?

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**Peter Oleksiak** - *DTE Energy - SVP and CFO*

No. We typically will grow the dividend in line with the earnings versus the amount. So the amount of equity we are issuing is not going to have an impact on our dividend decision.

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**Andrew Weisel** - *Macquarie Capital Securities - Analyst*

Okay. Thank you very much, guys.

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**Operator**

It appears there are no further questions at this time. I'd like to turn the conference back over to today's speakers for any additional or closing remarks.

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**Gerry Anderson** - *DTE Energy - Chairman and CEO*

Well, I will just wrap up by again thanking everybody for joining the call this morning. As I said at the outset, one quarter into the year, we feel very good about how things are progressing versus plan, both with respect to earnings and relative to a number of our key priorities.

Look forward to giving you all updates. We'll be down at AGA and a number of other conferences before we are back on a call like this for the midyear. So thanks for joining. Look forward to talking to you soon.

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**Operator**

This concludes today's call. Thank you for your participation. You may now disconnect.



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