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PNM Resources, Inc. (PNM)

Q2 2019 Earnings Call

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Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the PNM Resources Second Quarter 2019 Conference Call. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note, this event is being recorded.

I would now like to turn the conference over to Jimmie Blotter, Director of Investor Relations. Please, go ahead, ma'am.

Jimmie Blotter

Assistant Treasurer and Director, Investor Relations and Shareholder Services, PNM Resources, Inc.

Thank you, Nancy. And thank you, everyone, for joining us this morning for the PNM Resources second quarter 2019 conference call. Please note that the presentation for this conference call and other supporting documents are available on our website at pnmresources.com.

Joining me today are PNM Resources' Chairman, President and CEO, Pat Vincent-Collawn; and Chuck Eldred, our Executive Vice President and Chief Financial Officer; as well as several other members of our executive management team.

Before I turn the call over to Pat, I need to remind you that some of the information provided this morning should be considered forward-looking statements pursuant to the Private Securities Litigation Reform Act of 1995. We caution you that all of the forward-looking statements are based upon current expectations and estimates, and that PNM Resources assumes no obligation to update this information. For a detailed discussion of factors affecting PNM Resources results, please refer to our current and future annual reports on Form 10-K, quarterly reports on Form 10-Q, as well as reports on Form 8-K filed with the SEC.

And with that, I will turn the call over to Pat.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

Thank you, Jimmie. And good morning, everyone. Thank you for joining us today for our second quarter earnings call, and for National Ice Cream Sandwich Day.

So, let's begin on slide 4. Our GAAP earnings per share in the second quarter of 2019 reflect a loss of \$0.95 compared to earnings of \$0.48 in the second quarter of 2018. This was driven by the \$104 million after-tax write-off of items that were under appeal with the New Mexico Supreme Court following the order confirming their disallowance from rate base.

Ongoing earnings per share are \$0.37 compared to \$0.53 in the second quarter of last year. We reported in July that weather during the second quarter in New Mexico was the mildest in 20 years, significantly impacting our financial results. We are reaffirming our revised guidance of \$2.05 to \$2.11 that incorporates these results. Chuck will provide further details on the financials in a few minutes.

After the newly passed Energy Transition Act became effective in June, we filed our Consolidated Application on July 1 to request approvals for the abandonment, securitization and replacement power for the San Juan Generating Station. So, let's turn to slide 5 for the details on the filing.

The application requests the abandonment of San Juan after the participation agreements and coal supply contracts end in June of 2022, and it requests the issuance of \$361 million of energy transition bonds. The lower financing costs of these bonds provide a financial benefit to customers. The Energy Transition Act also benefits other stakeholders that are impacted by the transition out of coal. The total amount to be securitized by the bonds includes significant dollars in resources to assist the employees affected by the transition out of coal and the surrounding community that has relied on the coal plant in their economy for so long.

As for the replacement power, we filed multiple scenarios based on the interest shared by the parties during the legislative session, and we are continuing discussions with those parties to share the results from the models prepared by our team and those of third-party experts. In our modeling, we look to balance environmental impacts with the cost to customers and the reliability of our system. Our recommended replacement plan saves customers money, reduces emissions, provides for investment that generates property tax revenues in the San Juan area school district, and responsibly integrates new battery storage technology to maintain reliability on our system. It is also consistent with our goal of 100% emissions free energy by 2040.

The Commission bifurcated the filing and took its authorized time extensions providing for a nine-month schedule for abandonment and securitization, and up to 15 months for replacement power approvals. The hearing examiner set a schedule that has hearings on abandonment and securitization in December. For replacement power, the schedule accommodates an earlier consideration of the proposed PPAs with hearings in December, and then hearings on the remaining replacement power in March of 2020. We will provide updates on this case as it progresses throughout the year.

Before I turn it over to Chuck, let me walk through some other regulatory updates for both PNM and TNMP. At PNM, the New Mexico Commission decided to hear oral arguments on the remand of our 2015 general rate review from the New Mexico Supreme Court. The Supreme Court order was clear, and that the Commission's orders should be revisited only to remove the piece that disallowed recovery for any future decommissioning costs. The Commission has communicated that it intends to review the transcripts of the oral arguments and the Supreme Court court order prior to taking further action.

Moving onto the BB2 Transmission Project, the Commission granted the CCN for this project, while deferring the associated ratemaking treatment to a future rate review. This allows the project to move ahead according to schedule.

On the Western Spirit Transmission Line, FERC approved the incremental rate on July 9. Approval of the acquisition is required from both the New Mexico Commission and FERC, and we expect those decisions in the fourth quarter of this year.

At the end of May, we also filed for approval of our voluntary solar subscription program that is available to municipalities, tribal governments and large customers. We partnered with the City of Albuquerque on this program, and they signed on for half of the 50 megawatt facility that is being constructed on the Jicarilla Apache land in Northern New Mexico. Walmart is also supporting the program, signing on to take any capacity not committed by other local or tribal governments. We requested approval from the Commission by November of 2019.

I noted last quarter that PNM would file its annual renewable plan to request an update to rates under our renewable rider. The plan includes 140 megawatt PPA for wind power that is necessary to meet the 20% by 2020 Renewable Portfolio Standard. This wind power would rely on the BB2 Transmission Line to deliver it to our customers. Hearings have been proposed for November, and we would expect a decision in the first quarter of next year.

At TNMP, we filed for our second TCOS increase for 2019 on July 3, and it reflected a \$22 million increase in transmission rate base. The request reflects \$3.3 million of annual revenues that we expect to be effective in September of this year.

With that, I'll turn it over to Chuck for a detailed look at the numbers.

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

Thank you, Pat. Good morning, everyone. It's also a Happy International Beer Day.

I'll begin this morning on slide 8 with a recap of earnings and guidance. We issued a release in July discussing the impacts of weather on the second quarter. Our earnings for the quarter of \$0.37 are consistent with that information. As expected, PNM was significantly lower than second quarter 2018. While all the drivers are included in the appendix, the primary item to note is that the weather and load are down a combined \$0.15 from second quarter of last year. For TNMP, the drivers fully offset each other for the second quarter of 2019 versus 2018. Corporate and other was down \$0.01 compared to the second quarter of 2018.

As a result of the weather impacts at PNM, we revised guidance for the year. To address the earnings impact of the second quarter, we're able to implement mitigating plans for the remainder of the year. Our budgets are developed with flexibility and prioritized in a way that allow us to align our costs with revenues. Of course, the size of this impact was significant, so we're also offsetting this by managing the timing of when vacancies are filled, as well as lowering our results-based incentive compensation expense. We also saw strong market performance in our NDT, resulting in realized gains.

For 2019, we expect to have ongoing earnings per share of \$2.05 to \$2.11, targeting the midpoint of \$2.08. We have updated our quarterly EPS distribution for the third and fourth quarter expectations. We do not expect any of these items to impact 2020.

Now, turning to slide 9 for our load information. In our guidance range, PNM was the primary driver and you can see why we look at the degree days. PNM's cooling degree days were 37% lower than normal, and 53% lower than the second quarter of 2018. While we work to isolate the effects of weather, extreme periods will always have a distortion between load and weather. As we moved into July, we quickly saw a return to normal summer temperatures in New Mexico. TNMP has also had weather in the second quarter that was milder than the prior year, but it was roughly in line with normal.

Moving to load, we believe that these results are representative of the distortion between weather and load, and are not an indication of changes to the underlying economic situation. We continue to see announcements of businesses either moving into the state or expanding in both the private and public sectors adding jobs. Following the announcement of Netflix coming in New Mexico last year, there have been several other job announcements that are in our service territory. For example, NBCUniversal announced in June they're planning to also launch a 10-year venture in Albuquerque. Sandia National Laboratories announced in May that it plans to hire 1,900 employees by the end of the year. And Intel announced it plans to add over 300 jobs. There may be some timing shifts in our load as some of this growth comes online in the second half of the year.

At TNMP, our customers continue to exhibit strong demand, with new service requests continue to come in at an accelerated pace compared to last in the prior year. Changes in the timing into some of the interconnections expected this year have shifted from the first half of the year, but are expecting to bring these customers on line when they finish construction in the second half of this year or early next year. We may see results for the year in the lower range of load guidance at both PNM and TNMP as a result of these timing delays. However, we have factored this into our updated guidance range and the targeted midpoint of \$2.08.

Now, turning to slide 10. As Pat discussed, we made our San Juan filing on July 1. In our capital plan, we include the investments related to the recommended replacement power scenario. This represents a \$298 million investment, with \$278 million in generation and \$20 million in transmission.

In 2023, we haven't included amounts related to our remaining leases at Palo Verde. As these leases expire, we'll need to either purchase the leases to secure the capacity long-term or would need to consider the replacement capacity. This will be evaluated in the 2020 RFP process that started in July. This brings our total capital plan to \$3.6 billion from 2019 to 2023, and it represent rate base compound annual growth of 9.3% over the period.

I'll wrap up with our earnings power slide on page 11. The 2019 numbers shown reflect the revision of our guidance midpoint. Years 2020 to 2023 include the updates made in July to incorporate the recommended plan for replacement power in mid-2022. In 2022, we have a half-year of the San Juan rate base included before its retirement, and a half a year replacement power. 2023, shows the full-year impact of these changes. Proceeds from securitization will fund the replacement power, so no new additional financing is needed. I want to note that, as the replacement power is built in 2020 and 2021, we will need additional interim financing that will offset any earnings from AFUDC. When the energy transition bonds are issued in 2022, we'll be able to use those funds to pay out the interim financing for the replacement power.

Over the course of this plan, we continue to target 16% FFO-to-debt ratio, and holding company debt levels that are less than 20% of our consolidated debt. The growth at PNM and TNMP reflect our investment and the associated financing plans. We continue to be on track with our targeted growth range of 5% to 6% through 2023.

That concludes my remarks. And back to you, Pat. Cheers.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

Thank you, Chuck.

Before I begin questions, I want to [ph] make note the (00:15:07) collaboration and commitment from multiple stakeholders towards the common goal that led to the passage of the Energy Transition Act. The process for our San Juan filing is no different. To keep the spirit of collaboration moving forward, PNM [ph] plans (00:15:23) four scenarios for replacement power. We did this in acknowledgment of the competing interests in the Energy Transition Act. This innovative approach has been welcomed as a roadmap to continue the cooperation with these important stakeholders that was started by the ETA.

As part of that process, we have already held two community meetings, a specific session for parties running their own resource model, meetings with the Navajo Nation president and legislative committee, along with a special session for our own employees. In these meetings, we listened to concerns, shared data, and considered alternatives. So far, more than 523 people have participated in these meetings, and we only expect that number to grow.

This certainly isn't the easy way to do things as it takes incredible effort from our team and from the other parties. But this is too important to get wrong. So, thank you to everyone here at PNM Resources and all around New Mexico for committing your time and energy to this transition.

With that operator, let's open it up for questions.

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] And the first question comes from Greg Gordon with Evercore. Please, go ahead, sir.

Greg Gordon

Analyst, Evercore ISI

Q

Hey. Good morning.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Morning.

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Good morning.

Greg Gordon

Analyst, Evercore ISI

Q

I don't know if I can drink a beer while I'm eating my ice cream sandwich, but I think I'll give it a try.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Do try. Chuck's doing it, so.

Greg Gordon

Analyst, Evercore ISI

Q

Well, okay. There's safety in numbers then. There has been a little bit of confusion given reports sort of what the NMPRC is doing with regard to the bifurcation of the case, and some statements that have been made by commissioners with regard to the timing of these approvals, and perhaps some dissonance in the expectation of what may happen in these bifurcated proceedings. So, can you talk about your perspective on what flexibility the PRC has under the legislation to approve the securitization, not approve the securitization, that they have flexibility to approve a different amount, and then the flexibility they have under the law with regard to finding the least-cost or most balanced option ultimately for the replacement power?

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Yeah, Greg. I mean, we're very confident in our legal position at the ETA, including securitizations applies to our filing. And I think you saw that yesterday, Commissioner Fishman responded to Western Resource Advocates' motion, and moved up the date to get some responses back to August 9, because they know this is an important issue. So, all of Western Resource Advocates, the environmentalists also believe that we have a good position on this.

And if you look at the law for the securitizations, it's really a checklist of things that the Commission has to do. So, we are very confident in our position. And I think we're glad to see that the Commission is moving up the determination of that, because it is important as we move through this process.

Greg Gordon

Analyst, Evercore ISI

Q

And then, with regard to the different – the four different options you've presented, how under the law or under preexisting PRC precedent or standards are they sort of mandated to go about making that decision?

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Well, if you look at sort of preexisting and precedent, you would take what's kind of called the least-cost plan, but it also can take into account the environment [ph] and this reliability (00:19:38). And that's the Scenario 1 that we've presented. The law also shows a preference for resources up in San Juan. And that was the second scenario that we file. And then, the third and the fourth, we filed in response to some of the stakeholders' interests.

So, the Commission, I think, has the latitude to pick among those different scenarios as long as it does – it maintains reliability. The Commission does not necessarily have to pick that least-cost plan, because there is that flexibility for them to take into account the environment and then the law. The ETA gives them the flexibility to put resources up in San Juan school district.

Greg Gordon

Analyst, Evercore ISI

Q

Okay, clear. Thank you. Have a good day.

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Thank you.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Thank you, and enjoy the rest of your beer and ice cream sandwich.

Operator: The next question comes from Julien Dumoulin-Smith from Bank of America. Please, go ahead.

Alex Morgan

Analyst, Bank of America Merrill Lynch

Q

Hi. Good afternoon. This is Alex Morgan calling in for Julien. Thanks so much for taking my call.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Welcome, Alex.

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Welcome.

Alex Morgan

Analyst, Bank of America Merrill Lynch

Q

My first question, I know you mentioned a few things for cost-cutting expectations in 2019, mostly about the not filling vacancies and potentially lower bonus compensation. I was wondering if we should be thinking about any other cost-cutting metrics as well for this year?

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

No, I think that's really, as I mentioned, our plans are very flexible to align our revenues against the expenses in the business. As we think about the circumstance that happened in the second quarter, that gave us sufficient time to prioritize our budgets and use that flexibility to lay out a plan that we think and confident that we can execute.

But it was significant, as I mentioned, that changing guidance, we just don't have enough to cover the entire \$0.15 without making the guidance change. But with the changes and the focus on \$2.08 and the mitigating plans we put in place, we're confident we're back on track where we should be.

Alex Morgan

Analyst, Bank of America Merrill Lynch

Q

Okay. Thank you so much. And I was hoping that you could – I know, you discussed a little bit the additional equity or no need of that, because it more or less offsetting AFUDC. Could you just talk a little bit more about the financing plan as the replacement power comes back online for San Juan and then using the bonds to pay off the interim financing?

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Yes. So, if you reference the earnings power slide that we have in the appendix, it gives you some detailed notes of the financing plans, which include some equity financing that the business would plan about \$50 million in 2020 and \$100 million issued in 2021. And then, we have a \$300 million mandatory convert beginning the mid-2021. So, that's the underlying basic assumptions about our financing plans. But also, the proceeds we get out of securitization, those bonds will be used to pay off some interim financings that we have for the replacement power as we begin to pursue whatever decision comes out of the Commission in our ability to make those investments.

Alex Morgan

Analyst, Bank of America Merrill Lynch

Q

Okay. Thank you so much. Those are my questions. Have a great afternoon.

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Thank you.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

Thank you.

A

Operator: Our next question comes from Ali Agha from SunTrust. Please, go ahead.

Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

Thank you. Good morning.

Q

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

Good morning, Ali.

A

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

[ph] Good morning. (00:23:29)

A

Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

Good morning. First question, Chuck. I just wanted to be also a little more clear on the securitization aspect of the financing in the legislation. What's your sense, again, given some reports that the Commission doesn't seem to be giving a very clear indication on where they stand on securitization? There's some talk that they're trying to take a timeline that starts before the legislation was passed, so that somehow securitization doesn't come into play. Can you just give a sense of what you're seeing or hearing from the Commission? I guess part 1.

Q

And part 2, I understand your point that the legal side of it is very clear. But could there be a scenario where you get the wrong decision out of the Commission, you got to go to the Supreme Court, and ultimately get the right decision, but there's time lost during that process? So, I just wanted to get a little more perspective on what you're thinking.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

Sure, Ali. And obviously, we have not talked to the commissioners directly because this is a pending case. And I won't speculate on what was in the newspaper, because I don't know anything more than what was there.

A

But I'd say we are very confident of our legal petition and our legal position. And I think, as you saw, Commissioner Fischmann yesterday issued an order that asked for responses due on this matter by August 9, right? So, that moves up the uncertainty about it. And we can still go to the Supreme Court if we're not getting that certainty. Because we agree that the certainty is important, and we would rather have that sooner or later. So, we see Commissioner Fischmann's move as a good move. And if we don't get it soon, we will definitely consider going to the Supreme Court with some of our other supporters of the ETA.

Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

Q

And so, by moving this up to August 9, does that give you a timeline on do they expect to have a decision that very day? Or when would you expect them to clear this up?

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

No, we wouldn't expect a decision that very day, and they didn't set a date for a decision. But it's moved it up significantly because, for example, a hearing examiner have right now on their schedule, it would be August 23 that we have filings and responses due on October 18. So, they've moved the responses up – let's do my math – to two months. So, we would expect to have a decision relatively soon after that. Because everybody understands that we need to have clarity as we move along, and we would rather have a decision sooner rather than later. Because if it doesn't – if it says that [ph] it doesn't cover the act (00:26:07), we will obviously go to the Supreme Court on that.

Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Right. And my second question, Pat. Remind us, what's the timing for the next rate case filing in New Mexico? And given that you'll file that and then you will have another rate increase for the replacement power, how are you thinking about sort of back-to-back rate increases and the implications in New Mexico?

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Yeah. Ali, this is Chuck. We certainly have – we've indicated before our plans are to file something in December. That's currently our plan. But we'll continue to monitor that based on the progress and the focus that we have on this current pending case with abandonment. And we want to make sure that the resources and dedication and focus on that execution is really where our priority is. And then, subsequent to that, then we'll really determine the final plans for issuing – filing a new rate case. So, again, that's our current plan. But we'll consider it based on what we see as the progress in the process we go through abandonment filing.

Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

Q

I see. And to be clear, Chuck, there could be a scenario that instead of two cases, you kind of roll it all into one as part of the abandonment filing?

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

A

Well, it's too early to say what we might do and how we might think of it. I mean, securitization itself will lend itself to a certain amount of rate proceedings that are required to support the ETA. And then, beyond that, it's just a reflection of what our normal rate case needs are. And we'll just deal with that as we begin to see the process, and to Pat's point, in a more clear way, then we'll make the determination of what the appropriate filing should be.

Ali Agha

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you.

Operator: [Operator Instructions] Our next question comes from Paul Fremont from Mizuho Securities USA. Please, go ahead.

Paul Fremont

Analyst, Mizuho Securities USA LLC

Q

Thanks. Pardon me for being confused with the NMPRC. But I had thought that Commissioner Becenti-Aguilar had dismissed the Western Resource's petition. So, how does the Fishman order that was put out yesterday, does that represent a change in the Commission's position or is the original petition still rejected?

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

What happened, Paul, was WRA filed an interlocutory appeal after it was denied by Commissioner Becenti-Aguilar. So, this was a second filing by Western Resources Advocates that Commissioner Fishman is responding to.

Paul Fremont

Analyst, Mizuho Securities USA LLC

Q

So, does that mean that the Commission is going to essentially respond here or could they still come out with the same sort of response that Commissioner Becenti-Aguilar came out with basically just rejecting the appeal?

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

So, what they did was they responded differently, right, and said that they are going to hear, get responses on this on August 9. Now, they can respond differently than Commissioner Becenti-Aguilar did. So, what Commissioner Fishman said is, no, this is important, we got to hear this, and we want responses due on August 9. So, they could respond differently to what Commissioner Becenti-Aguilar did.

Paul Fremont

Analyst, Mizuho Securities USA LLC

Q

Okay. And then, in my understanding then from what you said is, if you get a definite or if there's a definite no then out of the Commission and they rejected again, then WRA or yourself would then be free to go to the courts. Is that...

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

That is correct.

Paul Fremont

Analyst, Mizuho Securities USA LLC

Q

Okay. I think that's it. Thank you very much.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

A

Thanks. You're welcome, Paul.

Operator: This concludes our question and answer session. I would now like to turn the conference back over to Miss Pat Vincent-Collawn for any closing remarks.

Patricia K. Vincent-Collawn

Chairman, President & Chief Executive Officer, PNM Resources, Inc.

Thank you. And thank you all again for joining us this morning. I hope you enjoy the rest of your summer. And whether you choose to celebrate National Ice Cream Sandwich Day or International Beer Day or both, please celebrate safely. Thanks. Bye-bye.

Charles N. Eldred

Chief Financial Officer & Executive Vice President, PNM Resources, Inc.

Don't eat too much ice cream.

Operator: The conference is now concluded. Thank you for attending today's presentation. You may now disconnect, and enjoy the rest of your day.

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