Q2 2016 Earnings Call

Company Participants

- David Mordy
- Joseph B. McGoldrick
- Scott M. Prochazka
- Tracy B. Bridge
- William D. Rogers

Other Participants

- Ali Agha, SunTrust Robinson Humphrey, Inc.
- Brian J. Russo, Ladenburg Thalmann & Co., Inc. (Broker)
- Charles Fishman, Morningstar, Inc. (Research)
- Insoo Kim, RBC Capital Markets LLC
- Jeremy B. Tonet, JPMorgan Securities LLC
- Lasan Johong, Auvila Research Consulting
- Michael Lapides, Goldman Sachs & Co.
- Neel Mitra, Tudor, Pickering, Holt & Co. Securities, Inc.
- Nick S. Raza, Citigroup Global Markets, Inc. (Broker)
- Steve Fleishman, Wolfe Research LLC

MANAGEMENT DISCUSSION SECTION

Operator

Good morning and welcome to the CenterPoint Energy's Second Quarter 2016 Earnings Conference Call with Senior Management. During the company's prepared remarks, all participants will be in a listen-only mode. There will be a question-and-answer session after managements' remarks.

I will now turn the call over to David Mordy, Director of Investor Relations. Mr. Mordy, you may begin.

David Mordy {BIO 20391499 <GO>}

Thank you, Ashley. Good morning, everyone. Welcome to our second quarter 2016 earnings conference call. Thank you for joining us today. Scott Prochazka, President and CEO; Tracy Bridge, Executive Vice President and President of our Electric Division; Joe McGoldrick, Executive Vice President and President of our Gas Division; and Bill Rogers, Executive Vice President and CFO, will discuss our second quarter 2016 result and provide highlights on other key areas. We also have with us other members of management, who may assist in answering questions following the prepared remarks.

In conjunction with the call today, we will be using slides which can be found under the Investors section on our website, centerpointenergy.com. For a reconciliation of the non-GAAP measures used in providing earnings guidance in today's call, please refer to our earnings press release and our slides, which, along with our Form 10-Q have been posted on our website.

Please note that we may announce material information using SEC filings, press releases, public conference calls, webcasts and posts to the Investors section of our website. In the future, we will continue to use these channels to communicate important information and encourage you to review the information on our website.

Today, management is going to discuss certain topics that will contain projections and forward-looking information that are based on management's beliefs, assumptions and information currently available to management. These forward-looking statements are subject to risks and uncertainties. Actual results could differ materially based upon factors, including weather variations, regulatory actions, economic conditions and growth, commodity prices, changes in our service territories, and other risk factors noted in our SEC filings.

We will also discuss our guidance for 2016. The guidance range considers Utility Operations performance to-date and significant variables that may impact earnings such as weather, regulatory and judicial proceedings, throughput, commodity prices, effective tax rates, and financing activities.

In providing this guidance, the company uses non-GAAP measure of adjusted diluted earnings per share that does not include other potential impacts such as changes in accounting standards or unusual items, earnings or losses from the change in the value of Zero-Premium Exchangeable Subordinated Notes or ZENS securities and the related stocks, or the timing effects of mark-to-market accounting in the company's Energy Service business.

The guidance range also considers such factors as Enable's most recent public forecast and effective tax rate. The company does not include other potential impacts such as any changes in accounting standards or Enable Midstream's unusual items.

Before Scott begins, I would like to mention that this call is being recorded. Information on how to access the replay can be found on our website. And with that, I will turn the call over to Scott.

Scott M. Prochazka {BIO 17360314 <GO>}

Thank you, David, and good morning, ladies and gentlemen. Thank you for joining us today and thank you for your interest in CenterPoint Energy. We will begin on slide four. This morning, we reported a second quarter 2016 loss of $2 million or $0.01 loss per diluted share compared with net income of $77 million or $0.18 per diluted share in the same quarter of last year. Second quarter 2016 earnings were impacted by several charges which Bill will discuss in greater detail later in the call.

On a guidance basis, second quarter 2016 adjusted earnings were $73 million or $0.17 per diluted share compared with adjusted earnings of $84 million or $0.19 per diluted share in the same quarter of last year.

The fundamentals of our Utility business segments remained strong. On a guidance basis, Utility Operations contributed $0.14 per diluted share in the second quarter of 2016 compared to $0.13 per diluted share in the same quarter of last year, improving $0.01 despite milder than normal weather at our electric utility. We continue to see strong customer growth in both our electric and gas utilities. Combined, our utilities added over 90,000 metered customers during the last 12 months.

Capital expenditures remained strong as we invest in the growth, safety and reliability needs within our service territories. Rate relief, driven by capital investment continues to be an important contributor to earnings growth.

To date, we have secured $45 million in annualized distribution investment recovery at our electric utility and $18 million in annualized revenue associated with recovery of capital investments at our Texas Gas Utilities. Further, we expect approvals in two gas rate cases in the third and fourth quarters. Joe and Tracy will provide additional regulatory updates for their business segments later in the call.

Turning to Midstream Investments, we have a number of highlights on slide five. Midstream Investments contributed $0.03 per diluted share in the second quarter of 2016 compared to $0.06 per diluted share in the same quarter of last year. The contribution was reduced as a result of losses attributable to changes in the fair value of commodity derivatives and an increase in deferred taxes. As I mentioned earlier, Bill will provide additional details on these items.

Enable's call highlighted the robustness of drilling activity in the SCOOP and STACK plays, which continue to be recognized as two of the top plays in the country. Enable continues to focus on strengthening their balance sheet, lowering cost, and improving capital efficiency. We believe they are well-positioned to take advantage of market opportunities over the next few years.

Turning to slide six, given the year-to-date performance and outlook for both Utility Operations and Midstream Investments, we are reaffirming full year earnings guidance of $1.12 to $1.20 per diluted share. 2016 earnings growth drivers include utility customer growth, capital discipline, rate relief, and operating and financing cost management.

CenterPoint's core strategy remains to operate, maintain and invest in our current utility service territories, deploying capital to address needs for system growth, maintenance, reliability, safety, and customer interactions.

In February, we announced that we would conduct two strategic reviews focused on possible incremental value creation for our long-term shareholders. One review contemplated placing utility assets in a REIT structure, with the assumption of executing a public offering of that REIT, and redeploying those proceeds on behalf of our shareholders. We have completed our REIT evaluation based upon assumptions for qualified assets, revenue requirements determined through general regulatory proceedings, and capital markets' considerations.

Key variables include the collection of federal income taxes within the revenue requirement, and the timing of adjustments to lease payments related to capital investments by the REIT on behalf of the utility operating company. We have concluded that current uncertainties, along with the complexity of the structure, do not warrant pursuit of a REIT. As always, we remain open to explore avenues for long-term value creation for our current shareholders.

The strategic review regarding our Enable ownership is ongoing, and we remain committed to providing an update on this subject before the end of 2016. As I mentioned before, our utility fundamentals continue to be strong and on track. We remain committed to our vision to lead the nation in delivering energy, service and value. We are focused on consistent performance including safe, reliable and efficient operations for our customers and long-term value creation for our shareholders.

Tracy will now update you on Houston Electric.

Tracy B. Bridge {BIO 17360316 <GO>}

Thank you, Scott. I am pleased with Houston Electric's performance this quarter. As you will see on slide eight, core operating income in the second quarter of 2016 was $135 million compared with $131 million for the same period last year. The business benefited from rate relief, customer growth, higher equity return primarily related to true-up proceeds and higher right of way revenues. These benefits were partially offset by higher depreciation in taxes, lower usage primarily due to milder weather and modestly higher O&M.

Similar to the first quarter of this year, higher depreciation was anticipated due to both the amount and type of capital invested. We continue to focus on keeping annual O&M growth under 2%, excluding certain expenses that have revenue offset.

Houston Electric added approximately 55,000 metered customers since the second quarter of last year. We continue to anticipate approximately 2% metered customer growth this year. As we've mentioned before, 2% customer growth equates to approximately $25 million to $30 million of incremental revenue annually.

Slide nine provides a regulatory update for Houston Electric. In April, we filed an application with the Texas Public Utility Commission for a DCRF interim rate adjustment. Our application requested the annualized revenue requirement be set at $49.4 million. In July 2016, a settlement was approved by the Commission, providing for an annualized revenue requirement of $45 million effective September 1, 2016. As a reminder, the amount is reset with each filing, so it is not additive to the approved DCRF revenue requirement from the prior filing.

Recently, Houston Electric was awarded the International Smart Grid Action Network Award of Excellence and the Global Smart Grid Federation Best Smart Grid Project. Through our smart grid deployment, key technology partnerships, and the dedication of our employees, we have reduced outages by more than 134 million minutes, enabled restoration of more than 1.5 million outage cases without a customer phone call, and saved millions of dollars in eliminated fees for more than 2.3 million metered customers in our service area. I am pleased to report Houston Electric's performance is on track for the year.

Although we experienced milder than normal weather in the second quarter, the third quarter to date has been warmer than normal.

Further, the third quarter has historically been the most impactful quarter for Houston Electric. We will continue to focus on the safety, reliability, and efficiency of our system to meet the growing needs of our service territory.

Joe will now update you on the results for gas operations.

Joseph B. McGoldrick {BIO 5483407 <GO>}

Thank you, Tracy. Our Natural Gas operations, which includes both our Gas Distribution business and our non-regulated Energy Services business, had a solid quarter. As you'll see on slide 11, operating income for our Natural Gas Utilities was $20 million compared to $19 million for the same period in 2015. Operating income was higher, primarily due to rate relief and continued customer growth. These increases were offset by higher depreciation in taxes, as well as increased contractor services expense, related to integrity services and increased credit and collection activities.

Customer growth remains strong in our Natural Gas Utilities, having added nearly 36,000 customers since the second quarter of 2015, almost identical to the growth in customers this time last year. This represents customer growth slightly in excess of 1%.

Slides 12 and 13 provide detail on 2016 regulatory developments, including our rate cases in Minnesota and Arkansas. The Minnesota PUC issued an order authorizing a $27.5 million rate increase, based on an ROE of 9.49%. We have had interim rates in effect since last fall, and we'll implement final rates later this year.

In the Arkansas case, a non-unanimous settlement was reached for an annual revenue increase of $14.2 million. The settlement includes the use of formula rate plan mechanism, starting in 2017, to recover future capital investment and expenses. The recommended ROE in the Arkansas settlement is 9.5%. The settlement is pending commission approval, and we expect the final order and new rates to be implemented in the third quarter.

As Scott mentioned, we have also finalized four Texas GRIP cases which collectively increase revenues $18 million on an annualized basis.

Turning to slide 14, operating income for our Energy Services business was $7 million for the second quarter of 2016 compared with $7 million for the same period last year, excluding a mark-to-market loss of $7 million and a gain of $2 million, respectively.

Our integration efforts from our recent acquisition are anticipated to be completed within 2016. With more than 12,000 new metered customers, Energy Services now has more than 30,000 customers. Inclusive of integration and acquisition costs, this year we anticipate the Energy Services business will roughly match last year's financial performance of $38 million in operating income, again, excluding mark-to-market adjustments. For 2017, the first full year of combined operations, we now expect Energy Services to provide annual operating income, excluding mark-to-market gains or losses, in the range of $45 million to $55 million.

Overall, our Natural Gas operations performed well this quarter. Excluding mark-to-market, year-to-date operating income is up $30 million or 7% higher than 2015 despite lower weather-related throughput at the utilities and acquisition and integration costs and Energy Services. We will continue to operate effectively and efficiently as we focus on growth, safety and the reliability of our system.

I will now turn the call over to Bill, who will cover financial performance and forecast.

William D. Rogers {BIO 3893186 <GO>}

Thank you, Joe, and good morning to everyone. I will begin on slide 16. We reported a second quarter 2016 loss of $0.01 per diluted share. Earnings included a charge of $110 million or $0.17 per diluted share associated with our ZENS Securities.

This charge is primarily due to the merger of Time Warner Cable and Charter Communications through a cash and stock sale and the related revaluation of associated assets and liabilities on our books. Further details on the accounting at the merger date on May 18 are provided on page 17 of the slide deck, as well as Note 11 in our second quarter Form 10-Q.

In addition, the quarter also included a $0.01 mark-to-market charge in our Energy Services segment. Therefore, our earnings per share on a guidance basis was $0.17 versus earnings of $0.19 per share for the second quarter of 2015. Earnings per share increased $0.01 for our Utility Operations segment and decreased $0.03 for our Midstream Investments. Midstream was impacted by losses attributable to changes in fair value of commodity derivatives.

As discussed on Enable's call and disclosed in their second quarter Form 10-Q, Enable uses derivatives to manage the partnership's commodity price risk. The accounting for these derivatives requires that the charges associated with the fair value of the instruments be recognized in current earnings.

In addition, at the CenterPoint level, we recognized an increase in deferred tax expense related to recent Louisiana tax law changes and our Enable income from Louisiana. The sum of these two factors reduced the Midstream per share contribution to our earnings by approximately $0.03.

Additionally, this was the first quarter that we recognized income from our investment in the Enable-Preferred as disclosed in Footnote 8 and within Other income. Assuming Enable declares this dividend on a going-forward basis, we expect to earn $0.03 per share in 2016 and $0.05 per share per year in future years.

As a reminder, second quarter has historically provided the lease contribution to our annual earnings. For the first two quarters of this year, we have delivered $0.49 in guidance earnings per share, consisting of $0.37 in Utility earnings and $0.12 in Midstream earnings. Given our performance year-to-date and ongoing strong Utility fundamentals, as Scott mentioned earlier, we are reiterating EPS guidance of $1.12 to $1.20. As shown on slide 18, we are also reiterating our target of 4% to 6% EPS growth in each of 2017 and 2018.

On slide 19, we provide an overview of our anticipated financing plans, interest expense and effective tax rate. Year-to-date, internally generated cash is strong, allowing us to fully fund capital expenditures and to pay dividends.

In the second quarter, our interest expense was lower on a period-to-period basis due to refinancing maturing debt at lower interest rates. During the quarter, we refinanced $300 million of short-term debt at Houston Electric with a five-year maturity at a coupon of 1.85%. We expect to refinance another $300 million of short-term debt at Houston Electric in the second half of 2016. Therefore, for the full-year 2016, we expect interest expense to be lower compared to 2015 with an EPS contribution of approximately $0.02.

Interest expense saving opportunities should also present themselves in 2017 and 2018. We have $1.15 billion in maturities in those years, and the weighted average coupon for this maturing debt is roughly 6.1%.

With respect to cash expense as a result of the deferred tax recognition for the Midstream segment income, we expect our effective tax rate to be 37% this year. This is higher than our previously stated anticipated tax rate of 36%.

In addition to our earnings release and our 10-Q filings for all of our registrants filed this morning, we would like to remind you of other press releases or filings of interest.

First, our Board of Directors declared a $0.2575 dividend per share on July 28, payable on September 9. Second, on July 21, we filed with the SEC an amendment to our Form 13D with respect to our ownership interest in Enable Midstream. The required update to our February filing reflects that we sent OGE a Right of First Offer, or ROFO, and that we will solicit offers from third parties to acquire our interest in Enable.

As stated in our press release earlier this year and in our Form 13D-A, we continue to evaluate a number of strategic alternatives for our investment in the partnership, including a sale, a spin-off, or maintain our ownership. As Scott stated, our intent is to provide an update on the review prior to the end of the year.

And with that, I'll turn the call back over to David.

David Mordy {BIO 20391499 <GO>}

Thank you, Bill. We will now open the call to questions. In the interest of time, I will ask you to limit yourself to one question and a follow-up. Ashley?

Q&A

Operator

At this time, we will begin taking questions. Thank you. Our first question comes from the line of Insoo Kim with RBC Capital Market.

Q - Insoo Kim {BIO 19660313 <GO>}

Just regarding the Enable strategy, I know you can't comment much on that, but with the ROFO notice that you provided to OGE, if they do make an offer for your stake in Enable in the coming weeks, how does that impact, if any, your ability to still potentially pursue the spinoff? Just wanted to make sure -- depending on what they say on the stake and whether you have some offers outstanding with other third parties, if that bounds you toward the sell option versus still having a spinoff option.

A - William D. Rogers {BIO 3893186 <GO>}

Insoo, good morning. It's Bill. The spin-off and the consideration of sale are two separate tracks. So if OG&E were to make an offer to CenterPoint for CenterPoint stakes, then, we are not obligated to accept that offer.

Q - Insoo Kim {BIO 19660313 <GO>}

Okay. So the two options are still open regardless of what they comeback with?

A - William D. Rogers {BIO 3893186 <GO>}

Correct.

Q - Insoo Kim {BIO 19660313 <GO>}

Understood. Okay. I know you guys can't comment much more on that, so I'll leave it there. But just moving to the electric utility, given customer growth has been above forecast for the past couple of quarters, how do you see the customer growth for the balance of the year and outlook for future years? I know you've mentioned 2% annual growth as sort of a target, but it seems like it's been trending a little bit higher.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yeah, Insoo. This is Scott. We continue to see a strong customer growth as you obviously noted and we posted in our results. We see all signs pointing to that continuing. We continue to track the leading indicators about housing development, and that continues to be strong. I will say that one area that may provide a little softening would be multifamily homes. That market is getting a little long here. But I think what that would do is that would probably tend to drive our growth rate from perhaps slightly above 2%, down closer to 2%, nothing that I would consider to be problematic. But that could be the downside piece of it. But other than that, we continue to see very strong local development.

Q - Insoo Kim {BIO 19660313 <GO>}

Got it. Thank you very much.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yes.

Operator

Thank you for your cooperation. Our next question is from Ali Agha with SunTrust.

Q - Ali Agha {BIO 22785216 <GO>}

Good morning.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Good morning, Ali.

Q - Ali Agha {BIO 22785216 <GO>}

Scott, first question, as you are continuing to look at strategically what to do with Enable, can you tell us what are some of the big milestones or what is it that you're looking at in terms of reaching your final conclusion for that? And related to that, if the sale option were to be exercised by you, have you been able to resolve the tax issue, or will that still be the same as you've talked about in the past?

A - Scott M. Prochazka {BIO 17360314 <GO>}

Ali, I'll provide a little bit of comment on this. I'll let Bill comment on the tax piece of it. But our options are essentially the same as we communicated in the past, and that is to look at a sale or a spin.

The timing is such that – as we've indicated, we're just continuing to step through the process. Providing the ROFO notice to OGE was one step in the process. And so we're just going to continue marching down that path, with the expectations that we'll be able to provide an update to you all by – certainly by the end of the year. Bill, would you like to comment on the tax question?

A - William D. Rogers {BIO 3893186 <GO>}

Certainly. Good morning, Ali. The tax consideration is still there. As we've discussed, we have negative basis in our investment in Enable Midstream, and, therefore a sale for cash would result in a significant taxable gain.

Q - Ali Agha {BIO 22785216 <GO>}

Okay. And the sale option, I guess, that reminded me, and you mentioned that, sale for stock would still be an option within that sale option.

A - William D. Rogers {BIO 3893186 <GO>}

Yes. So there's potential to defer an eventual recognition of the gain through a sale for stock or some other currency. We would likely get there if we went on that structure through a reorganization under the tax code.

Q - Ali Agha {BIO 22785216 <GO>}

Okay. And last question, Scott, there's a lot of consolidation going on – on the regulatory front both in the gas and electric side. Just wanted to get a sense of what your current view is as you're looking at the landscape around you and other opportunities that you guys could potentially capitalize on?

A - Scott M. Prochazka {BIO 17360314 <GO>}

Ali, yes. I certainly observed the same thing you are, and that is that there have been a number of consolidations. The strategy that we have is still very much centered around the investment we can make in our utilities in our current service territories. So our focus continues to be around the $1.3 billion-plus we're spending on our own utilities and growing those utilities to meet the needs of our customers and grow our earnings along with that.

Q - Ali Agha {BIO 22785216 <GO>}

Thank you.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yeah.

Operator

And your next question comes from the line of Michael Lapides with Goldman Sachs.

Q - Michael Lapides {BIO 6317499 <GO>}

Hey, guys. I think Dave is going to hate me because I have a couple of them for you. One is simple. In your multiyear – your EPS growth rate guidance for 2017 and 2018, do you assume Enable earnings contribution grows, shrinks or stay flat in that period? I'm trying to just kind of think about the puts and take between utility, regulated utility earnings growth versus kind of consolidated EPS growth.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Michael, as you know, Enable has not put out any information beyond this current year. That said, we have looked at a number of possible growth rates that could come from Enable, and we've tested that against our capabilities at the utility, and combined, under a number of different scenarios, we feel comfortable that we can achieve that 4% to 6% rate.

Q - Michael Lapides {BIO 6317499 <GO>}

Got it. So even if Enable were to decline in 2017 and 2018, you're still pretty comfortable getting the 4% to 6% consolidated growth rate.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yes. We've looked at – like I said, Mike, we've looked at a number of scenarios, and one of them would be one where the growth rates have not returned for that segment as they had been in the past.

Q - Michael Lapides {BIO 6317499 <GO>}

Got it. One question on the Houston business, the CEHE business. I want to make sure I understand the DCRF. The $45 million, what is the incremental amount that's going into rates in September of 2016?

A - Tracy B. Bridge {BIO 17360316 <GO>}

Michael, this is Tracy. We don't think about it as an incremental amount because every year, the revenue requirement is determined on a standalone basis. You might recall that a year ago, we implemented a rate increase of $16 million, and now we're going to be implementing a rate increase of $45 million, but the two are not related because we calculate the revenue requirement independently every year. So, if you're modeling it, just put in $45 million on an annualized basis starting September 1, 2016.

Q - Michael Lapides {BIO 6317499 <GO>}

Yes. But I got to know what's in your current numbers, right, because otherwise we could be overstating – we could be completely misstating. So I'm just trying to make the bridge here.

A - Tracy B. Bridge {BIO 17360316 <GO>}

So the revenue for 2016 for DCRF would be $16.2 million, and the revenue for 2017 would be $53.8 million. Okay?

Q - Michael Lapides {BIO 6317499 <GO>}

Got it. So that makes sense. And then the agreement to go from $45 million to $49 million, so does that just imply, and I'm being very simplistic here, a $4 million step up?

A - Tracy B. Bridge {BIO 17360316 <GO>}

Yes.

Q - Michael Lapides {BIO 6317499 <GO>}

I assume that's what that is, but I'm just making sure I'm understanding that correctly.

A - Tracy B. Bridge {BIO 17360316 <GO>}

That's what it implies, yes.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yeah. So, Michael, that would be a $4 million step up assuming we did not make another DCRF filing next year.

Q - Michael Lapides {BIO 6317499 <GO>}

So this doesn't preclude you from making another DCRF filing next year?

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yeah. That's correct. Right. We can make another filing next year. And then we would go through a whole new determination, and then it would be a new number that would be in place of the $45 million that's here today.

Q - Michael Lapides {BIO 6317499 <GO>}

I appreciate that. Thank you, Scott. Much, much, much, much more clear there. Much appreciate it.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yes.

Operator

And your next question comes from the line of Steve Fleishman with Wolfe Research.

Q - Steve Fleishman {BIO 22027192 <GO>}

Guys.

A - William D. Rogers {BIO 3893186 <GO>}

Good morning, Steve.

Q - Steve Fleishman {BIO 22027192 <GO>}

Just a clarification on disclosure maybe. When OGE responds within their 30 days on the ROFO, either way, would that be something you're going to disclose what their response is?

A - William D. Rogers {BIO 3893186 <GO>}

Steve, we'll look at the required disclosure at that time, and that, of course, would depend on their response.

Q - Steve Fleishman {BIO 22027192 <GO>}

Okay. So it's possible they could not make an offer, we just wouldn't know?

A - William D. Rogers {BIO 3893186 <GO>}

That's correct.

Q - Steve Fleishman {BIO 22027192 <GO>}

Okay. And then my understanding is, just to be clear, once they've responded, either way, you then have 120 days to basically transact and, after which, the process starts again. Is that right?

A - William D. Rogers {BIO 3893186 <GO>}

Yes. Just to put some clarity on that, Steve, they have 30 days to respond to the ROFO. If they did not respond, then we would move forward with a solicitation of offers, although we're not precluded from doing that at this time. If they did respond, then we would have 30 days to respond to their offer, and then subsequent to that, we would have the 120 days.

Q - Steve Fleishman {BIO 22027192 <GO>}

Okay. That's great. And then just on the mark-to-market hit that you took on the Enable hedges, do you expect that will come back to you by the end of the year?

A - William D. Rogers {BIO 3893186 <GO>}

Steve, again it's Bill. If nothing happened other than the forward curve staying the same at June 30, and they didn't enter into any more hedges, as it played out much but not all of that would come back in 2016 with a balance in 2017. But should gas prices go higher, under mark-to-market accounting that could impact what Enable records, or should it go lower or go the other way. So it very much depends upon where gas prices are at each quarterly statement period.

Q - Steve Fleishman {BIO 22027192 <GO>}

Okay. Got it. Thank you.

Operator

And your next question comes from the line of Neel Mitra with Tudor, Pickering.

Q - Neel Mitra {BIO 16431920 <GO>}

Can you guys hear me?

A - William D. Rogers {BIO 3893186 <GO>}

Yeah. Good morning, Neel.

Q - Neel Mitra {BIO 16431920 <GO>}

I had another question around Enable and the possible tax leakage from a sale. If OGE were to make an offer that you would accept, would the same tax consequences arise as if it were a third-party buyer? Would you still be on the hook for the negative tax basis, or is there something different about OGE being a buyer?

A - William D. Rogers {BIO 3893186 <GO>}

Neel, it's Bill. Good morning. There's no difference between OGE and any other buyer with respect to tax consequences.

Q - Neel Mitra {BIO 16431920 <GO>}

Okay. Great. And I noticed in the presentation that you noted that you wouldn't need equity for 2016 and 2017, but I wanted to just understand under what scenario you could possibly need equity 2018 and beyond. Would it be that you found additional growth projects that would kind of put you at the top or above the 6% growth rate at the utilities, or is it something else, or do you feel that you don't need any equity at all until the end of the decade or further?

A - William D. Rogers {BIO 3893186 <GO>}

Neel, here's how do we get to our thinking on equity. We take a look at our credit metrics, principally FFO to debt, and we're currently at approximately 20%. We want to maintain that because we like our credit ratings. Admittedly, we think we have some debt capacity within that. But if that were to erode, then we would consider equity. And that could erode from any number of factors, including, as you said, a higher rate of capital investment.

Q - Neel Mitra {BIO 16431920 <GO>}

Okay. And with the Enable stake, if that were to decline, would that be something that would cause you to issue equity, or do you view that as a separate entity that's self-funding?

A - William D. Rogers {BIO 3893186 <GO>}

Enable, in 2015, was under 20% of our cash flow in the way we think about our internally generated cash flow. So it's significant but we'd have to take a look at what the credit metrics would be for us and what that might imply for equity at that time.

Q - Neel Mitra {BIO 16431920 <GO>}

Okay. Got it. Thank you very much.

Operator

And your next question comes from the line of Jeremy Tonet with JPMorgan.

Q - Jeremy B. Tonet {BIO 15946844 <GO>}

Just want to follow up on the Enable situation, and if you were to sell your stake there and receive stock against that, and then you were to subsequently distribute that stock, would that introduce tax leakage as well, or would that be a way to mitigate that?

A - William D. Rogers {BIO 3893186 <GO>}

Good morning, Jeremy. I'm going to restate what you posited, and then if I don't get that right, correct me. But you're assuming we would sell for stock and would not have a taxable recognition at that time, and then we would spend whatever we received out to shareholders. Is that correct?

Q - Jeremy B. Tonet {BIO 15946844 <GO>}

Yes, spend it out to shareholders. That's right.

A - William D. Rogers {BIO 3893186 <GO>}

Right. So we have not contemplated that strategy. I think that would have some combination of the tax effects you would either have in a sale for stock and a spin.

Q - Jeremy B. Tonet {BIO 15946844 <GO>}

Okay. Thanks. And just with the whole strategic review process here, I'm just wondering if you could help us into your thought process. While the commodities have softened a little bit recently, it seems like the cycle has turned a bit. So, I'm just wondering how that enters into the calculus of your decisions here with the cycle getting better?

A - William D. Rogers {BIO 3893186 <GO>}

Well, it certainly is nice to see the commodities turning around as they have, but we went into this evaluation geared at looking for alternatives to reduce the volatility associated with this earnings stream. So, we're continuing our process. We're going to continue through even as commodities are improving because we want to see if there's a way to reduce that volatility in a way that could create value for our shareholders.

Q - Jeremy B. Tonet {BIO 15946844 <GO>}

Great. Thanks. And then one just quick one. Correct me if I'm wrong, but I think there was a slug of the energy resources debt $325 million that matured in May. I was just wondering what happened to that, if that was refinanced or if we should take any meaning from that?

A - William D. Rogers {BIO 3893186 <GO>}

You're correct. $325 million did mature in May. We met that maturity with cash flow generated at CERC (39.00) and short-term borrowings. As I said on March on this call, we were cash flow positive for this first six months of the year, including investments on CapEx on behalf of our customers and including dividends paid to our shareholders.

Q - Jeremy B. Tonet {BIO 15946844 <GO>}

That's helpful. Thank you very much.

A - William D. Rogers {BIO 3893186 <GO>}

Yeah.

Operator

And your next question comes from the line of Brian Russo with Ladenburg Thalmann.

Q - Brian J. Russo {BIO 6238768 <GO>}

Just to clarify, is OGE required to respond with a yes or a no, or can they just not respond and that's just an implied no?

A - William D. Rogers {BIO 3893186 <GO>}

Brian, good morning. It's Bill. The latter is correct. They can stay silent.

Q - Brian J. Russo {BIO 6238768 <GO>}

Got it. Okay. And then also to clarify, the decision not to pursue the REIT structure for the Texas assets, does that conclude all strategic alternative reviews, or are there other options that you're looking at?

A - William D. Rogers {BIO 3893186 <GO>}

Brian, that concludes our strategic review of the concept of a REIT for utility assets, but our other review underway is the consideration around our Enable ownership. And as we've said, that's still ongoing.

Q - Brian J. Russo {BIO 6238768 <GO>}

Okay. But there's no ongoing review of your gas LPCs (40:28)?

A - William D. Rogers {BIO 3893186 <GO>}

That's correct.

Q - Brian J. Russo {BIO 6238768 <GO>}

Okay. Thank you.

Operator

And your next question comes from the line of Nick Raza with Citi.

Q - Nick S. Raza {BIO 20528692 <GO>}

Thanks, guys. Really a couple of just housekeeping items. In terms of the marketing business or Energy Services business that you acquired, when you acquired it, you said that combined with your existing operations and the acquisition, you'd generate anywhere from $40 million to $50 million in operating income. That number seems to be a little higher now. Could you just talk about that real quick?

A - Scott M. Prochazka {BIO 17360314 <GO>}

Joe, do you want to take that one?

A - Joseph B. McGoldrick {BIO 5483407 <GO>}

Sure. Good morning, Nick. This is Joe. Yes, that's correct. We have increased that guidance for our Energy Services business, given the integration of the business and some improved performance at our CES base business, so we are now comfortable that we will be in the $45 million to $55 million range in the first full year which is 2017.

Q - Nick S. Raza {BIO 20528692 <GO>}

Okay. And then I guess one of the aspects that you mentioned that would help you meet your EPS guidance in the outer years is O&M or operating cost reductions or not as much growth. But if I look at your O&M expenses, they seem to have been growing by about 5%. Can you just talk about what's driving that and how you guys view that?

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yeah. So the 5% that you see on the chart includes some items that have revenue offsets. So if you back that out and you consider some timing aspects of spend on a quarter-to-quarter basis, we're still confident we can manage this expense in that around 2% to 3% range.

Q - Nick S. Raza {BIO 20528692 <GO>}

Okay. That's all I have. Thank you, guys.

A - Scott M. Prochazka {BIO 17360314 <GO>}

Yeah.

Operator

Your next question comes from the line of Charles Fishman with Morningstar.

Q - Charles Fishman {BIO 4772353 <GO>}

Hey, Bill, just based on your comment, the effective tax rate, the 37% was really just a one-time thing and – just assuming business as usual with respect to Enable going forward from a modeling standpoint, still 35%, 36% would be a long term rate?

A - William D. Rogers {BIO 3893186 <GO>}

Yes. I would advise using 36% per our provision. It's just going to be 37% this year due to the change in Louisiana Law.

Q - Charles Fishman {BIO 4772353 <GO>}

Okay. And then second question was for Tracy. Right away revenues, remind me or – I mean I know they're going down, but are we still talking $10 million in total this year? I forgot what you've said in the past.

A - Tracy B. Bridge {BIO 17360316 <GO>}

Good morning, Charles. We're projecting $10 million to $20 million of right-of-way in miscellaneous revenue this year.

Q - Charles Fishman {BIO 4772353 <GO>}

$10 million to $20 million, which is still an elevated level over normalized, correct?

A - Tracy B. Bridge {BIO 17360316 <GO>}

Well, it depends on what you mean by normalized. Certainly, 10 years ago and beyond that, it would be much lower, but we've had some pretty strong miscellaneous revenues in the last few years, as you recall.

Q - Charles Fishman {BIO 4772353 <GO>}

Right. Okay. That's all I had. Thank you.

A - Tracy B. Bridge {BIO 17360316 <GO>}

Thank you.

Operator

And your next question comes from the line of Lasan Johong with Auvila Research.

Q - Lasan Johong {BIO 4135934 <GO>}

I guess, it's still good morning in the East Coast. The ZENS issue, does it make sense to buy back given the low current interest rate environment?

A - William D. Rogers {BIO 3893186 <GO>}

Lasan, good morning. It's Bill.

Q - Lasan Johong {BIO 4135934 <GO>}

Good morning.

A - William D. Rogers {BIO 3893186 <GO>}

This remains a very low-cost source of capital for us. If we were to think about buying back the bet, we would have recognition from a tax perspective associated with the capital gain that we've otherwise deferred.

Q - Lasan Johong {BIO 4135934 <GO>}

I see. I understand. Okay. Next question, I guess, is for – well, I guess it's for anybody who wants to answer it, but the hot weather in that area tends to get super hot, and I understand it's approaching 100-degree weather, so maybe Tracy is the best person to ask this question. Are you guys having any issues with infrastructure overheating or melting down, or having any kind of equipment problems even with trucks or anything like that?

A - Tracy B. Bridge {BIO 17360316 <GO>}

Good morning. We're not. The system is holding up very well. Unlike some parts of the country, we're accustomed to this humidity, and so the system is holding up fine. Thank you for asking.

Q - Lasan Johong {BIO 4135934 <GO>}

Excellent. I guess this question goes back to Bill, my last question. Is there any way you can engineer a light kind of exchange for Enable, I mean, essentially, to avoid the big tax bill now?

A - William D. Rogers {BIO 3893186 <GO>}

There are ways to continue to defer recognition of taxes if we sold for stock or units of another entity, but it would not be through a like-kind exchange. It would be through a reorganization within the tax code.

Q - Lasan Johong {BIO 4135934 <GO>}

Okay. So you couldn't take cash for Enable and then, say, buy pipeline or buy gas utility somewhere and transfer your basis over that way?

A - William D. Rogers {BIO 3893186 <GO>}

We do not see a path in that direction.

Q - Lasan Johong {BIO 4135934 <GO>}

I understand. Thank you for your help.

Operator

Thank you for your cooperation. And we do have a follow-up question from the line of Michael Lapides with Goldman Sachs.

Q - Michael Lapides {BIO 6317499 <GO>}

Cash taxes, I know you talked about the effective tax rate, but how long do you expect not to be a cash taxpayer for?

A - William D. Rogers {BIO 3893186 <GO>}

Michael, it's Bill. We will be a cash taxpayer. It's just that it's at a very low rate. We expect to be a cash taxpayer this year as measured by cash income taxes paid divided by accrual income before taxes – and that number will be in the high-single digits.

Q - Michael Lapides {BIO 6317499 <GO>}

And then for how long – like how big do you – how big is your effective whether it's in NOL or a like balanced weather-generated via bonus D&A or something else, how long do you expect to be a very low cash taxpayer for?

A - William D. Rogers {BIO 3893186 <GO>}

It will gradually creep up to 35% over the planning horizon. In terms of cash tax rate, that of course will be impacted by the level of capital investment and depreciation rates amongst all the other factors that go through our tax return.

Q - Michael Lapides {BIO 6317499 <GO>}

So kind of getting closer to a normal GAAP in the cash tax rate by the next two to three years or kind of longer term than that?

A - William D. Rogers {BIO 3893186 <GO>}

Longer than that, Michael, at the end of our five-year planning horizon.

Q - Michael Lapides {BIO 6317499 <GO>}

Got it. Thank you, Bill. Much appreciated.

A - David Mordy {BIO 20391499 <GO>}

Thank you, everyone, for your interest in CenterPoint Energy. We will now conclude our second quarter 2016 earnings call. Have a nice day.

Operator

And this concludes CenterPoint Energy's second quarter 2016 earnings conference call. Thank you for your participation.