Q2 2020 Earnings Call

Company Participants

- Brian X. Tierney, Executive Vice President and Chief Financial Officer
- Darcy Reese, Managing Director, Investor Relations
- Nicholas K. Akins, Chairman, President and Chief Executive Officer

Other Participants

- Andrew Weisel, Analyst, Scotiabank
- Durgesh Chopra, Analyst, Evercore ISI
- James Thalacker, Analyst, BMO Capital Markets
- Jeremy Tonet, Analyst, JPMorgan
- Paul Patterson, Analyst, Glenrock Associates
- Sophie Karp, Analyst, KeyBanc Capital Markets

Presentation

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the American Electric Power Second Quarter 2020 Earnings Call. At this time, all lines are in a listen-only mode. Later, we will conduct a question-and-answer session, instructions will be given to you at that time. (Operator Instructions) And as a reminder, today's conference call is being recorded.

I would now like to turn the conference over to Darcy Reese. Please go ahead.

Darcy Reese {BIO 20391516 <GO>}

Thank you, Cynthia. Good morning, everyone, and welcome to the second quarter 2020 earnings call for American Electric Power. We appreciate you taking the time to join us today. Our earnings release, presentation slides and related financial information are available on our website at aep.com. Today, we will be making forward-looking statements during the call, there are many factors that may cause future results to differ materially from these statements, please refer to our SEC filings for a discussion of these factors.

Joining me this morning for opening remarks are Nick Akins, our Chairman, President and Chief Executive Officer; and Brian Tierney, our Chief Financial Officer. We will take your questions following their remarks.

I will now turn the call over to Nick.

Nicholas K. Akins {BIO 15090780 <GO>}

Okay, thanks, Darcy. You're welcome everyone to American Electric Power's second quarter 2020 earnings call. While we continue to see the effects of COVID-19 pandemic, AEP has responded well with not only ensuring the safety of our employees and redefining the business processes to accommodate the changed environment and reducing our cost in response to lower revenues, but we also responding to hurricane and storm activity to ensure the safe and reliable service to our customers. Our team at AEP Texas with support from internal, external resources performed well through hurricane Hanna to restore power to over 200,000 customers during that recent weather event and we are now supporting recovery efforts in the Northeast as well.

While COVID cases escalated in some areas, we continue to engage our employees on safe practices to prevent the virus spread both at work and outside of work to set an example in our communities. On the financial front, our operating earnings performance has been strong in the face of these challenges. AEP's operating earnings came in for the quarter at $1.08 per share, bringing our year-to-date operating earnings to $2.10 per share versus $1 share for second quarter '19 and $2.19 per share year-to-date 2019.

We are reaffirming our originally stated guidance range of $4.25 to $4.45 per share and our 5% to 7% long-term growth rate. AEP is also adjusting our capital upward during the five-year capital forecast period from $33 billion to $35 billion to accommodate the North Central Wind project addition. Also as we stated in the last quarter earnings call, we have continued to evaluate the short-term deferral of $500 million in our 2020 capital program that we talked about last quarter and we are placing $100 million back into the 2020 plan at this point. So all in all, a constructive quarter given the headwinds of the economy due to COVID. In fact, we continue to make progress toward our target of achieving at least the midpoint of the guidance range.

As far as load is concerned, we continue to see the arbitrage between residential load and negative industrial and commercial load during the quarter as we continue to look for leading indicators as to the health of the state economies, we have been pleased to see the new customer connections remained stable and in some jurisdictions, increasing from 2019 levels. Looking forward, we expect to see a continued shift to a certain degree from residential load back to commercial and industrial albeit these shifts will be dependent upon the nature of the pandemic recovery.

During the COVID-19 crisis, we continue to take all appropriate measures to ensure the safety of our employees, both in the field and for those who can work from home. Temperature testing, masking requirement, social distancing and hygiene have become the normal course of business in this environment. While our offices are open to employee meetings and certain other activities, we are still asking our employees who can work from home to remain home most likely through the end of the year. This has not slowed the progress, however, toward redefining our business processes going forward.

Our Achieving Excellence Program is now back in full swing with the added dimension of work from home learnings that will enable us to define even more efficiencies than previously considered. We also late last year completed initial analysis of what a 21st century technology framework would look like and with the addition of Therace Risch, a former JCPenney, EVP, Chief Information Officer, to our team. She has by the way hit the ground running. I'm confident the nexus of her efforts around the IT and other technologies married with Achieving Excellence, COVID learnings and other strategic initiatives will enable us to further define operating efficiencies that will benefit our customers and shareholders.

We are on track for the $100 million of cost reductions for this year as we adjust to expectations regarding revenues due to COVID-19 and the first quarter weather deficiencies that we had. And after reviewing our July weather, we have partially made up for the weather issue that we talked about during the first quarter, so we are making progress within the guidance range expectations and we are now targeting the midpoint of our guidance. As we move closer to 2021 and the addition of North Central Wind, we will still be disappointed not to be in the upper half of our 5% to 7% long-term growth rate.

I would like to spend a little time taking -- talking about steps we are taking to internally consider the effects of the recent and ongoing discussions about race in America. AEP is not only engaged externally with various local and national organizations, but we were also open to very frank and open dialogue internally. We call it our seize the moment action plan, this plan includes engagement with our leaders and employees in the organization through internal discussions, external speakers, webcast, including myself to be posted internally and process changes that will continue to make AEP a strong committed company that enables all of our employees to contribute in an open and transparent fashion.

We have a great culture at this company, but we can always do better by understanding the impacts of stereotypes, different perspectives based upon life experiences, the burden placed on employees of color in our organization and what systemic racism versus individual racism actually means. I believe the dialogue will enable a much deeper discussion that will benefit our diversity and inclusion efforts as well as enable AEP to be a better partner to our communities as we effectuate lasting change.

We can't talk about these cultural attributes without also realizing what our brand projects externally. And that brings me to the second issue that we at AEP certainly believe affects our brand, that would be the issue surrounding Ohio House Bill 6 legislation. Let me start by saying that we are not aware of any information suggesting that AEP's participation in the process was anything other than lawful and ethical. We have a robust code of ethics and regularly communicate our expectations to our employees so that they conduct all business, including advocacy on public policy issues with integrity, honesty and in compliance with the law. We consistently advocate for policy positions that benefit our customers, communities and shareholders and our advocacy of HB 6 was no different.

We ultimately supported the legislation because we believe it maintained important fuel diversity for Ohio, including support for investments in renewables, nuclear generation and two coal plants operated by OVEC. We were surprised and disappointed to learn of what federal investigators allege was a scheme by the speaker of the Ohio House and others to enrich themselves and we, along with you, have been trying to educate ourselves about the criminal complaint and the underlying conduct in it. There has been a lot of speculation and media reports about the identity of various unnamed companies described in the affidavit in support of the compliant. Based on the facts that we know, we do not believe that AEP is any of the companies, specifically described in the affidavit. We have not been contacted by any authorities conducting the investigation. If at any point we are, we will cooperate fully.

I would also like to discuss 501(c)(4) organizations more generally. AEP has contributed to a variety of 501(c)(4) social welfare organizations to promote economic development and educational programs across our service territories. One such organization is empowering Ohio's economy, which was organized to promote economic and business development in Ohio. Starting in 2015, AEP contributed a total of $8.7 million to empowering Ohio's economy. For a view of publicly available tax forms, followed by empowering Ohio's economy, shows that it made a number of grants over time to a wide variety of charitable organizations under 501(c)(3) and social welfare organizations under 501(c)(4).

Our contributions to empowering Ohio's economy to support its mission were appropriate and lawful. Given the ongoing legal proceedings surrounding HB 6 that we are still learning about and that we are unaware of any allegations of wrongdoing involving AEP. I'm going to let those proceedings play out rather than commenting further on this subject.

We also understand the concerns that some have expressed regarding the lack of transparency surrounding 501(c)(4) organizations, which are not required to disclose their donors and amounts donated to them. With that in mind, we will commit to include additional disclosures in our Corporate Accountability Report with respect to contributions that we made to 501(c)(4) organizations in 2020 and going forward. We also are reviewing best practices in working to improve our policies and processes around political contributions and contributions to 501(c)(4) entities.

Regarding any repeal and replacement of HB 6, we are fully prepared as we have done previously to engage in whatever dialogue needs to occur to chart a path in Ohio toward a balanced energy portfolio that moves toward a clean energy future for Ohio. AEP has been very clear since the beginning of the nuclear debate that we were concerned about forging a path toward the adoption of renewables such as solar and wind, along with other technologies such as storage to mobile technologies to big data analytics to enable a smarter and more efficient grid. HB 6 has some of that, but we were also following HB 247 to move Ohio forward from a clean energy technology perspective.

If HB 6 is repealed in a way that appropriately reverses its effects, the financial impact is minimal to AEP. We already had several years of recovery for the OVEC units, HB 6 elongated that, we will continue to recover our energy efficiency contracts entered into before the legislation. AEP Ohio is already decoupled in many respects and we will continue to pursue bilateral solar and wind projects with customers. As we have said since day one, if our customers are expected to help put the bill for nuclear, they should also have the opportunity to take full benefit of renewables and movement to a clean energy economy and be able to access technologies that will help them to lower their electric bills.

Unrelated to HB 6, but an item that should not be lost in the Ohio legislature, is continued interest in promoting greater broadband access, particularly in rural Ohio. This is an area that we are well positioned to help stimulate by providing middle mile services to ISPs to advance a service for those communities. We are optimistic that the broadband legislation that passed the

House with broad support continues forward. As the pandemic has shown the digital divide is real and getting more pronounced than the need for broadband access for our customers, particularly rural customers is desperately needed and we can leverage into our communication system to make broadband access a reality.

We have already begun pilots in Virginia and West Virginia and certainly, with our large amounts of -- need for large amounts of data from the grid for monitoring and analysis purposes, tangentially providing mid-mile broadband accessibility is clearly a benefit to our communities.

On the regulatory front, our base rate case in Ohio was filed earlier this year, where we're seeking a net revenue increase of $41 million, a 10.15% ROE and continuation of outdoor and Enhanced Service Reliability Rider. We expect the procedural schedule to be set next month. In Kentucky, we filed our base rate case in July, which should conclude by year-end, we have sought $65 million with a 10% ROE as well as AMI deployment within the state. We sought to be creative in our use of ADFIT funds to help lessen the rate impacts to customers in the state.

I am pleased to report that the Texas Commission approved the AEP Texas DCRF settlement agreement, increasing revenue requirement by approximately $39 million, which reflects the $440 million of distribution investment placed in service in 2019. Throughout our territory, new customer interconnects continue to be strong in much of our service territory and several areas exceeding what we have seen in recent years. While the virus continues to challenge this nation, this provides hope in American commitment and ingenuity will continue to help fuel our recovery.

Lastly, we are extremely pleased to have now received all necessary regulatory approvals to move the full North Central Wind investment forward for the benefit of our customers. Although the disappointing PUCT denial of our application results in the project benefits not extending to our Texas customers, we received approvals from the Arkansas Public Service Commission and the Louisiana Public Service Commission in May for their portion and a flex-up option. Approval of flex-up option was designed to enable the full value of the project to go forward even if a state elected not to take advantage of the opportunity.

We are pleased that the Arkansas Public Service Commission and the Louisiana Public Service Commission, along with the Oklahoma Corporation Commission recognize the value of these projects and we look forward to delivering this value to Arkansas, Louisiana and Oklahoma customers. With regards to the project schedule due to the COVID-19 pandemic, we expect a minimal delay in the completion of the 199-megawatt Sundance project and expect the project to be delivered in the first quarter of 2021 instead of December 2020.

The other two projects are currently expected to be delivered by the developer by the end of '21 -- 2021. We are pleased to report in May, the IRS provided an extra year to the four-year continuity safe harbor related to production tax credit eligibility. So we have an additional year of flexibility should there be any delays to deliver these projects and achieve full value for our customers.

Now looking at the equalizer graph on page 5 of the presentation. Our overall regulated operations' ROE is currently 9.1%. We'd like to target a range overall of 9.5% to 10%. So I'll go into some of the things around weather and the other things that come into play. AEP Ohio -- the ROE for AEP Ohio at the end of second quarter was 11.1%, their ROE was above authorized due to favorable regulatory items in a transmission true-up, partially offset by the roll off of legacy fuel and capacity carrying charge recoveries. We expect the year-end ROE to trend around authorized levels of 10% as we maintain concurrent capital recovery of distribution and transmission investment.

In June 2020, as I said earlier, we filed the rate case in Ohio. As far as APCo is concerned, the end of the second quarter was 9.3% ROE, that ROE was below authorized due to lower normalized usage and higher depreciation from increased capital investments. Virginia's first triennial review was filed in March 2020 and covers the '17 to '19 periods and that case is currently ongoing. At Kentucky Power, the ROE is down to 5.7%, it was below authorized due to loss of load from weak economic conditions and loss of major customers along with higher expenses. Transmission revenues were also lower due to the delay of some capital projects. In June 2020, Kentucky Power filed a new base rate case seeking a $65 million revenue increase and an ROE of 10%.

I&M came in at 10.6% for the quarter, the ROE was above authorized due to continued management of O&M expenses, reduced interest expense and rate true-ups, partially offset by lower normalized usage. I&M's ROE is projected to trend towards 10% at year-end, consistent with authorized ROEs. PSO came in at 9.4% for the quarter, their ROE is right in line with the authorized level due to the management of O&M expenses, offset by lower normalization usage. PSO's 2019 base case approved the transmission tracker, a partial distribution tracker and an ROE of 9.4%, so everything is going well there.

SWEPCO came in at 8.3% and again, is below authorized due to loss of load and the continued impact of the Arkansas share of the Turk Plant, which accounts for about 110 basis points. SWEPCO received an order in its Arkansas-based settlement in December 2019 that's effective in January 2020, approving a $24 million increase and an ROE of 9.45%. AEP Texas came in the quarter at 7.4%, their ROE was below authorized due to lag associated with the timing and we've discussed this earlier at last quarter of the annual cost recovery filings and one-time adjustments from our recently finalized base rate case.

Favorable regulatory treatment allows AEP Texas to file annual DCRF and bi-annual TCOS filings to recover costs on significant capital investments. So while earnings should improve in 2020 with the base rate case finalized and annual filings now resumed, continued levels of investment in Texas will continue to impact the ROE as well. AEP transmission came in at 9.8%, it was below authorized primarily driven by the annual revenue true-up in the second quarter of 2020 and to return the overcollection of 2019 revenues. Transmission is forecasting an ROE of 9 -- in the range of 9.9% to 10.3% for 2020, so that should continue on as the year goes forward.

As I've mentioned in the past, our organization is undertaking a comprehensive view of our O&M and capital spending efficiency under a program that we coined Achieving Excellence. I'm excited about this opportunity for our employees because it goes to the heart of how we do work, removing past barriers that may have existed and looking at our processes through a different lens. We are now moving into the implementation phase of this initiative with opportunities for increased O&M savings and increased efficiencies in our capital spending being implemented over the next three years and beyond. This work will serve as the platform and help to integrate other initiatives around organizational design, digitization and in-process efficiency and work from home initiatives.

The program will also be a precursor to our annual budgeting process in the future. We will share more information about these initiatives and the expected O&M savings later this year, but we have recently jump started this initiative by offering an early retirement incentive program for a targeted set of our employees. The program has recently closed and I'm pleased to say that we have reached our goals of this initiative, where about 200 of our employees have selected to take this incentive to retire. I am thankful to those who will be leaving the company soon for many reasons. One, for their years of service and dedication to AEP and for providing the Company an opportunity to take advantage of organizational design changes upon their exit. I'll be providing more detail when we wrap up all these initiatives later this fall.

Before I turn this over to Brian, particularly with the headwinds we all face today, I'd like to paraphrase some of the lyrics from the song Lost In The Echo by the rock group, Linkin Park, that I think represents AEP today. Now this may take a little time for you to figure out what I'm saying here, but nevertheless, the lyrics say, we don't hold back, we hold our own. We can't be mapped, we can't be cloned. We can't see flat, it ain't our tone.

What you get from AEP is our consistent focus on being a positive tone, attitude and performance that will help our communities and customers get through this pandemic and the culture issues that scar our society. We will continue to be uniquely qualified to bring stakeholders together to move toward a clean energy future for our customers and again, provide the quality dividends and earnings that our shareholders expect.

Brian, I'll turn it over to you.

Brian X. Tierney {BIO 15917272 <GO>}

Thank you, Nick, and good morning, everyone. I will take us through the second quarter and year-to-date financial results, provide an update on how we're thinking about 2020, including a look at July load and finish with a review of our balance sheet and liquidity.

Let's stop briefly on Slide 6, which shows the comparison of GAAP to operating earnings for the quarter and year-to-date periods. GAAP earnings for the second quarter were $1.05 per share compared to $0.93 per share in 2019. GAAP earnings through June were $2.05 per share compared to $2.10 per share in 2019. There is a reconciliation of GAAP to operating earnings on pages 15 and 16 of the appendix.

Let's turn to Slide 7 and look at the drivers of quarterly operating earnings by segment. Operating earnings for the second quarter were $1.08 per share or $534 million compared to $1 per share or $494 million in 2019. Operating earnings for Vertically Integrated Utilities were $0.55 per share, up $0.17, driven by lower O&M and higher transmission revenue, primarily due to true-ups. Normalized retail load was favorable due to higher margin residential sales, more than offsetting significant decreases in industrial and commercial sales. We will talk more -- in more detail about our expectations around normalized load for the year later in the presentation.

Other favorable items included weather and rate changes. These positive items were partially offset by higher depreciation and other taxes and lower wholesale load AFUDC and off-system sales. The Transmission and Distribution Utility segment earned $0.29 per share, up $0.02 from last year. Both O&M and transmission revenue were favorable due to the impact of the transmission true-up on the segment. Increased transmission investment in ERCOT was positive as well. Rate changes were also favorable and partially offset by prior-year Texas carrying charges, the roll off of legacy riders in Ohio, depreciation, lower normalized retail load and higher interest expense.

The Transmission Holdco segment contributed $0.19 per share, down $0.12, due to the impacts of the annual true-up and a prior-year FERC settlement. Our fundamental return on investment growth continued as net plant increased by $1.5 billion or 17% since June of last year. Generation and marketing produced operating earnings of $0.11 per share, up $0.05 from last year. A gain on the sale of Conesville and land sales contributed to the increase in generation business and the renewables business grew with the acquisition of multiple renewable assets. These increases along with the timing around income taxes, more than offset lower retail margins. Finally, corporate and other was down $0.04 per share, primarily driven by higher taxes related to consolidating items that were reversed by the year end and partially offset by lower O&M.

Let's turn to Slide 8 and review our year-to-date results. Operating earnings through June were $2.10 per share or $1 billion compared to $2.19 per share or $1.1 billion in 2019. Looking at the drivers by segment. Operating earnings for Vertically Integrated Utilities were $1.05 per share, up $0.04. Earnings in this segment increased due to lower O&M and higher transmission revenue, similar to the quarter as well as the impact of rate changes across multiple jurisdictions. Weather was unfavorable, primarily due to warmer than normal winter temperatures. Other decreases included higher depreciation, tax expenses and lower expected wholesale load, AFUDC, normalized retail load and off-system sales.

The Transmission and Distribution Utility segment earned $0.53 per share, down $0.05 from last year, primarily driven by a reversal of a regulatory provision in Ohio. Other smaller drivers included higher depreciation, the roll off of legacy riders in Ohio, prior year Texas carrying charges, higher interest expense and unfavorable weather. These items were partially offset by higher rate changes, the Ohio Transmission true-up impact on both O&M and transmission revenue and recovery of increased transmission investment in ERCOT.

The AEP Transmission Holdco segment contributed $0.47 per share, down $0.10 from last year for the same reasons identified in the quarterly comparison. Generation and marketing produced $0.18 per share, up $0.04 from last year. The growth in the renewables business and gains on generation more than offset the lower retail margins and timing around income taxes. Finally, corporate and other was down $0.02 per share due to higher interest expense and taxes related to consolidating items that were reversed by the year end and offset by a prior year income tax adjustment. Partially offsetting these items is lower O&M.

Turning to Slide 9. Let's review the assumptions we shared during the first quarter earnings call to reaffirm our 2020 operating earnings guidance range of $4.25 per share to $4.45 per share. As shown on the top line, we revised our retail sales projection from 1.5% growth in 2020 to a 3.4% decline by the year -- end of the year. For the second quarter, our sales growth in total was on target with the revised projections. The mix of sales growth is slightly different than projected but to-date, load is closely tracking to the revised forecast.

The second item was the impact of weather. While the first quarter weather produced a significant drag, the second quarter weather was slightly favorable. In addition, we experienced warmer than normal weather in July, especially in the East. As a result, we are now assuming less of a negative impact to our 2020 results from weather. The third item was managing our untracked O&M expense. We had originally planned to drive down O&M costs in 2020 to $2.8 billion from $3.1 billion in 2019. During the first quarter call, we shared that in response to the expected decline in sales, we now plan to reduce spend by an additional $100 million by aggressively managing O&M. We are on track to hit our projections through both, one time and sustainable reductions.

Finally, on the first quarter call, we identified approximately $500 million of capital expenditures that could be shifted out of 2020 and into future years. This was in anticipation of the potential impact of the economic downturn on cash receipts. Through the second quarter, our day sales outstanding have only marginally increased. We have brought about $100 million of the $500 million back into 2020 and we'll maintain flexibility as we move through the balance of the year.

Given the progress made on these key assumptions in the second quarter, we are able to reaffirm our 2020 operating earnings guidance range. There remain items that could positively or negatively impact our projections for the second half of the year, but we are confident in our ability to manage our way through various scenarios.

Now let's turn to Slide 10 to provide an update on our normalized load for the quarter. Starting in the lower-right corner, our second quarter normalized load was down 5.9%. This was consistent with the expectations we shared with you in the first quarter. We anticipated a significant contraction in the second quarter, followed by a gradual recovery over the second half of the year. Through June, our normalized sales were down 3.1%.

In the upper-left quadrant, our normalized residential sales increased by 6.2% in the second quarter. Year-to-date residential sales were up 1.9% compared to last year. We saw significant increases in our residential load during the stay-at-home provisions that were in effect during the quarter. Even after our states began their phased openings, we saw strong growth in weather normalized, residential sales across all jurisdictions. This was -- would suggest, many of our customers have continued to work from home. We expect the spike in residential growth to moderate as the commercial and industrial sectors improve during the second half of the year.

Moving clockwise, our normalized commercial sales decreased by 10.1% in the second quarter, bringing the year-to-date decline to 5%. Prior to COVID, we had experienced consistent improvement in our commercial sales over the past year. State imposed stay-at-home provisions challenged many of our commercial customers. All of our leading sectors experienced a drop in normalized load in the quarter, with the biggest declines coming in schools, churches, restaurants and hotels. Should our states manage without having to shut down businesses again, we expect commercial sales to gradually improve throughout the balance of the year.

Finally, in the lower-left chart, industrial sales decreased by 12.4% in the quarter, bringing the year-to-date decline to 6.6%. A number of factors have changed the outlook for this class but the biggest driver is the overall drop in economic activity. The industrial sales -- the industrial sectors that posted the biggest decline for the quarter were transportation equipment manufacturing, mining and primary metals. The two sectors that have grown in 2020 were pipeline transportation and petroleum and coal products.

Let's take a look at weather normalized load history and forecast in more detail on Slide 11. The chart on the left shows that for the second quarter, actual load very closely tracked our revised forecast. As you can see from the chart, our revised forecast assumed an economic trough in the second quarter that will gradually improve over the course of the year. So far, we are on track and we'll keep you updated as we move throughout the year. We wanted to time this call in order to give you the most updated load information through July. The chart on the upper-right shows monthly total weather normalized sales from March through July. Sales for our system were lowest in May and have shown improvement in June and July.

Total normalized load for May was down 8.6% versus June, which was down 4.8% versus July, which was down only 2.4%. The monthly macro data from both, the business and household surveys, show that unemployment rates peaked in April and have improved since. This was consistent with our assumption that the trough is behind us and the economy should continue its gradual improvement through the balance of the year.

The bottom-right chart shows that for the month of July, the trend that we forecast for the balance of the year is on track, although there are some differences in load mix to what we had predicted. Our overall load is tracking very closely to our revised forecast. Normalized residential sales for July, while still very positive at 4.3%, were less than for the second quarter and both commercial and industrial sales show real improvement versus the second quarter as shown on the prior page.

Now let's move to Slide 12 and review the company's capitalization and liquidity. Our debt to total capital -- our debt to capitalization ratio improved 70 basis points in the second quarter to 61.1%. This was largely attributable to reducing our short-term debt levels in conjunction with fortifying our liquidity position as we navigated the capital market turbulence in March. In fact, our liquidity position stood strong at $2.9 billion at quarter end. The short-term reduction actions also helped improve our FFO to debt ratio when compared to the first quarter, moving to 14.1% from 12.5% on a Moody's basis.

Our qualified pension funding remained flat at 93% and our OPEB funding increased approximately 5% to 135%. A falling discount rate increased both plans' liabilities during the quarter, but strong asset returns, especially in equities were able to offset the growth in liabilities. Let's wrap this up on Slide 13 so we can get to your questions. We are reaffirming our existing 2,000 operating earnings guidance of $4.25 to $4.45 per share. We are on track to reduce our O&M by the additional $100 million we announced last quarter, in response to the economic downturn and revised load implications. Of the $500 million of CapEx that we shifted out of 2020 into later years, we have now returned $100 million into this year. We will maintain our flexibility on this issue as we manage through the balance of the year.

We obtained regulatory approvals in Oklahoma, Louisiana, Arkansas and FERC and are moving forward with our $2 billion North Central Wind project in Oklahoma, benefiting our customers in PSO and SWEPCO. We have updated our capital plan from 33 -- our five-year capital plan from $33 billion to $35 billion, as well as our cash flow and credit metrics, which are provided on page 40 of the appendix. Because of our ability to continue invest in our own system organically, we are reaffirming our stated long-term growth rate of 5% to 7%.

With that, I will turn the call over to the operator for your questions.

Questions And Answers

Operator

Thank you. (Operator Instructions) And our first question will come from the line of Jeremy Tonet with JPMorgan. And your line is open.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Jeremy.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Hi, good morning.

A - Brian X. Tierney {BIO 15917272 <GO>}

Good morning.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Hi. Thanks for taking my questions here.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Just want to start off by a couple of, I guess, opposing items, influencing AEP going forward here. North Central Wind getting over the finish line, obviously a big positive, COVID headwind, on the other side here. Just wondering if you could talk a bit more about how these two factors influence, I guess, your 5% to 7% range with North Central Wind? I think, we're just looking to see if that could really help you here or just want to see how everything was shaken out I guess, going forward.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. so I mean, we look at -- and as Brian mentioned, on the COVID activity and the load activity, you're seeing residential load be pretty strong. And certainly, as you look forward, I think, residential load is going to continue to look strong with the work-from-home environment and the business cases that are developed afterwards. And then, if you have commercial and industrial pick up as well, it could be a positive from a financial standpoint.

The other regarding North Central and other wind projects and solar projects, we have a real opportunity to transition to that clean energy economy going forward in our service territory and that will really makes us -- again, we would be disappointed not to be in the upper part -- upper half of the 5% to 7% range, because you have to be bullish about not only where load is going, but also, in terms of the transformation from a -- just a pure and simple energy policy perspective regardless of who is in the White House in the next election, we'll continue moving toward a clean energy economy.

And then also, I think, bolstered by the other opportunities we have whether it's mid-range of broadband or other types of activities, electric vehicles and so forth, that we're going to see the further electrification of the society. So I'm really bullish about this company, in particular, but as well the industry.

Q - Jeremy Tonet {BIO 15946844 <GO>}

That makes sense. That's helpful, thanks. And maybe just kind of building off that with my second question. I think AEP is guiding to $1.3 billion of equity issuance at the fund North Central at this point. Just wondering, if you could update us there on your thoughts with regards to, is this definitely the path or is there the potential for portfolio optimization, is that still an option?

A - Brian X. Tierney {BIO 15917272 <GO>}

Yeah.

Q - Jeremy Tonet {BIO 15946844 <GO>}

I guess, how do you think about...

A - Brian X. Tierney {BIO 15917272 <GO>}

It absolutely is still an option and we're looking at all those options to see how to best finance it. We have plenty of time to make those things happen. Nick said that Sundance might be pushed out to the first quarter of 2021, but we're not going to see the rest of those projects coming in, Traverse and Maverick until the end of '21. So all those things are in play, whether it's equity or rotation of capital. But for planning purposes, we were guiding people to two-thirds equity for that project in aggregate.

Q - Jeremy Tonet {BIO 15946844 <GO>}

Got you. That's very helpful. Thank you.

A - Brian X. Tierney {BIO 15917272 <GO>}

Thanks, Jeremy.

Operator

Thank you. Our next question comes from the line of Andrew Weisel with Scotiabank. And your line is open.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Andrew.

Q - Andrew Weisel {BIO 15194095 <GO>}

Good morning. First a question on dividends. So at the end of the deck, you showed dividends in 2022, $1.5 billion versus $1.4 billion previously. I also see the footnote that dividend should grow with earnings. My question is, is that increase of $100 million a function of more shares outstanding after the North Central Wind equity or does it imply a step-up in dividend per share along with a step-up in EPS or perhaps both?

A - Nicholas K. Akins {BIO 15090780 <GO>}

I think, it'd be some of both because obviously, with North Central additional equity involved there, but also, as you said, I mean, our dividend will move with our earnings capability. So I'd say both.

Q - Andrew Weisel {BIO 15194095 <GO>}

Okay, great. Next from me.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Brian, do you have any comments on -- okay.

A - Brian X. Tierney {BIO 15917272 <GO>}

No, go ahead.

Q - Andrew Weisel {BIO 15194095 <GO>}

Please go ahead.

A - Nicholas K. Akins {BIO 15090780 <GO>}

No, I was seeing if Brian wanted to comment on that, but he said I covered it.

Q - Andrew Weisel {BIO 15194095 <GO>}

Okay, great.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Andrew Weisel {BIO 15194095 <GO>}

On CapEx, you mentioned that you're pulling back $100 million of the deferred CapEx. I just want to under -- be sure I understand what drove that. Is that a function of specific projects being more necessary or more appealing or is it more a function of the better than expected cash flows?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, I think that's a positive story. Some of that is related to our new customer connections and so, it was clearly evident that we needed to move that forward. But also, we had the capability financially to move it forward. We talked about this last time, the deferral of the $500 million, we weren't changing the five-year capital plan, we were going to maintain that level and the $500 million was merely being deferred, so that we could understand what the COVID issues were going to be. And so, we're continually looking at our process going forward in terms of putting that $500 million back in, in various stages. So what you saw this quarter was the first stage of that.

Q - Andrew Weisel {BIO 15194095 <GO>}

Very good. If I could just have one more here to clarify the last question from Jeremy. The 5% to 7% range, you're pointing to the upper end of that, is that a function of North Central Wind now being included or is it more that you're pointing to the higher end with or without North Central Wind as a one-timer?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Well, certainly we looked at North Central, but obviously, we continue to track and we believe that the upper half of that guidance range is certainly achievable and something that we again would be disappointed not to be able to get there. So that's clearly an opportunity for us and based on the things that I talked about earlier.

A - Brian X. Tierney {BIO 15917272 <GO>}

It should. North Central Wind should certainly solidify our position in the upper half.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah. And keep in mind too. At the same time, the Achieving Excellence Program is continuing to grow. So we already have plans in place and you're seeing sort of a crescendo of savings associated with that plan. And the first year 2020 is -- some of it's in there, but not much. And when you look at the future years, that continues to grow substantially and certainly, as I've mentioned earlier, the addition of two ACE and the focus on digitization, automation in combination with the learnings from COVID, I think is going to further accentuate the benefits from Achieving Excellence.

Q - Andrew Weisel {BIO 15194095 <GO>}

That all sounds great. Thank you so much.

A - Brian X. Tierney {BIO 15917272 <GO>}

Yeah.

Operator

Thank you. Our next question comes from the line of James Thalacker with BMO Capital Markets. And your line...

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, James.

Q - James Thalacker {BIO 1794957 <GO>}

Hey, good morning, guys. Can you hear me?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yes. I hear you. Yes. Good morning.

Q - James Thalacker {BIO 1794957 <GO>}

Okay, great.

A - Brian X. Tierney {BIO 15917272 <GO>}

Good morning.

Q - James Thalacker {BIO 1794957 <GO>}

Real quick question. I know you had outlined the bending the cost curve EI down to kind of $2.8 billion and as COVID took over, we are now down at $2.7 billion. It seems like year-to-date, if you just look at it on a after-tax basis, you guys are already kind of running above that kind of $100 million sort of run rate. How should we, I guess think about the non-tracked O&M versus the additional O&M that you are actually pulling out in response to COVID? And as we think about 2021, is there any guidance I guess, you could give us on how much of that you think will be retainable as we move into the next year?

A - Brian X. Tierney {BIO 15917272 <GO>}

Yeah. So, we're at this point, James, not able to provide obviously specific guidance on 2021. But I'll say, the incremental $100 million that we're able to garner is a combination of sustainable and one-timers and I think, it's a matter of managing our way through the downturn in normalized load and just working as hard as we can to pull out all the stops to make sure that we meet our commitments to shareholders and really target the middle part of that range without impacting customers, and so far we've been able to do that.

There have been some unexpected things that we've seen, maybe some things that aren't line items in O&M that have come out and I think, as you have things like traveling expense, conventions that people go to, things like that, meals, just buildings' expense that you have, things that just don't happen when everyone's working from home that I think are more like one-timers, that as people go back to work, we'll start to put those things back into place. But you've seen our track record over the last nine or 10 years now and it's been keeping a very, very tight range on untracked O&M and we're using those skills that we've learned over the last several years to make sure that we're able to manage our way through this circumstance.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, I would say -- and as Brian mentioned, I mean there's a lot of learnings from COVID-19 and the impacts and how we've operated and the efficiency of which we've operated and I think it sort of changes the perspective and changes the threshold of even what one-timers are and ongoing, because I think, the learnings we have from the year, we're going to be much different in our approach related to many of these activities. And actually, you would be surprised and I'll certainly talk about this more at the end of the year of what Achieving Excellence is showing us, the things that were buried in the organization that we obviously have an opportunity to take advantage of. And so, there's no question that you should expect a continued efficiency around the savings of O&M. And that's in the non-tracked area.

A - Brian X. Tierney {BIO 15917272 <GO>}

You've seen on page 34 of the presentation, you've seen the tight range we've been able to keep it in. In terms of bending the curve, as we go down to $2.7 billion and untrack, we actually are bending that curve downward at this point.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yes. I'm bending the warping, so that's good.

Q - James Thalacker {BIO 1794957 <GO>}

No, that's great. And I guess, just as a follow-up, I mean obviously, the run rate has been very, very good. I mean, you did a heroic job I guess in 2Q just the bulk of it from year-to-date perspective has kind of showed up, but as you move through the rest of the year, do you feel like you have additional room whether it'd be one-time or again, Nick, like you're talking about through just kind of change in workflow to continue to sort of press that down if you need to, if we get sort of resurgence in COVID again?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, I think, number one, really I'll think about -- the processes are in place and the focus of the organization is in place to be able to adjust. And I'm perfectly happy with the foundation that's been put in place for this organization on an ongoing basis. I mean, because if we look at our Achieving Excellence Program, it's not just a one-time program, it's a regular process we're going to go through in budgeting and it's also, a regular process that will go throughout the year for us to be able to adjust. So we will do what we have to do and there is no question that we have the foundation to be able to do it.

Q - James Thalacker {BIO 1794957 <GO>}

Okay, great. Well, thank you for taking my question and best of luck guys.

A - Brian X. Tierney {BIO 15917272 <GO>}

Yes, sure.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Thanks.

Operator

Thank you. Next we will go to the line of Durgesh Chopra with Evercore ISI. And your line is open.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Hey, good morning.

A - Nicholas K. Akins {BIO 15090780 <GO>}

So there is -- Hello?

Q - Durgesh Chopra {BIO 20053859 <GO>}

Hey. Can you hear me? I'm sorry.

A - Brian X. Tierney {BIO 15917272 <GO>}

Yeah, I hear you.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yes.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Great. Okay, great. Just I wanted to follow up on the O&M $100 million number. What of that $100 million was actually achieved in the quarter?

A - Brian X. Tierney {BIO 15917272 <GO>}

It will be -- the O&M CapEx for the O&M -- Oh, I'm sorry, O&M cuts. It's going to be achieved ratably throughout the balance of the year. So from second quarter, third and fourth, think about it being achieved ratably as we work our way through that.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Understood. And I apologize, there is like a echo in my -- in -- when I'm speaking. So and then the potential labor initiatives that you outlined, is that an addition to the $100 million?

A - Brian X. Tierney {BIO 15917272 <GO>}

It's all incorporated to get us to that $2.7 billion number.

Q - Durgesh Chopra {BIO 20053859 <GO>}

Understood, guys. Thank you so much.

A - Brian X. Tierney {BIO 15917272 <GO>}

Sure thing.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Thank you.

Operator

Thank you. Our next question comes from the line Sophie Karp with Keybanc. And your line is open.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Sophie.

Q - Sophie Karp {BIO 19699392 <GO>}

Hi. Good morning, guys. Good morning...

A - Brian X. Tierney {BIO 15917272 <GO>}

Good morning.

Q - Sophie Karp {BIO 19699392 <GO>}

Congrats on the quarter.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Thanks.

Q - Sophie Karp {BIO 19699392 <GO>}

And thanks for the time. I'm just curious about maybe, I can ask you more of a high-level question. Given the landscape -- market landscape that we are seeing right now, do you see an opportunity, maybe, an opening to do some rotation in your portfolio of assets maybe high grade it a little bit, if you will, and divest some and is there an opportunity for M&A for a more wired focus or like assets and tax evaluation?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, Sophie.

Q - Sophie Karp {BIO 19699392 <GO>}

Tax expense[ph]. I want to hear just your thoughts on that.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, sure. We've certainly been consistent in the discussion around any M&A activity or in terms of what we can do in terms of rotation, that's always an option that's available to us. And this company is moving toward a portfolio management approach where obviously, we have sources and uses and those sources include the assets we have and certainly, we will continue to look at those as opportunities and tie them with investments that we make. So we will continue to do that.

Regarding M&A activity, we have a high threshold, because we certainly have the ability to invest, we have the ability to -- we have the largest transmission system in the country. Certainly, our investment, our distribution businesses are continuing to grow considerably and so, if we can invest that without a premium, that's a good thing for our shareholders. Now that being said, we look at strategic areas that make sense to us, but certainly that threshold is high and we'll continue to evaluate that. But make no mistake that this company is focused on its ability to continue to grow but grow efficiently for our shareholders and we'll continue to do that.

Q - Sophie Karp {BIO 19699392 <GO>}

Thank you.

A - Brian X. Tierney {BIO 15917272 <GO>}

Yes.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Thank you.

Operator

Thank you. Our next question will come from the line of Paul Patterson with Glenrock Associates. And your line is open.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Good morning, Paul.

Q - Paul Patterson {BIO 1821718 <GO>}

Hey, how are you doing?

A - Nicholas K. Akins {BIO 15090780 <GO>}

All right. How are you?

Q - Paul Patterson {BIO 1821718 <GO>}

I'm managing.

A - Nicholas K. Akins {BIO 15090780 <GO>}

So am I.

Q - Paul Patterson {BIO 1821718 <GO>}

That's all we can do, I guess. So I don't think of you guys as being a primary beneficiary or primarily impacted by HB 6, but is there any ancillary or anything we should think about with the potential repeal of HB 6 in Ohio that could impact you guys?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Well, certainly, with the repeal, it's how it's replaced, is the issue and obviously, how it's repealed, because there are some things, some interconnections that occurred between HB 6 and the regulatory process, where we had regulatory recovery for areas that we need to make sure that's a clean transition that occurs, but on its face, the issues that were involved with that for us should be pretty well taken care of. So that's why we're saying it should be a minimal issue for us.

I think it's more of an opportunity for us, because if we're able to and really, if the state focuses on a clean energy economy going forward, that's going to provide us some opportunities to really do this the right way, including nuclear for the -- for our customers going forward.

Q - Paul Patterson {BIO 1821718 <GO>}

But if it's not replaced just because we don't know what's going to happen legislatively...

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Paul Patterson {BIO 1821718 <GO>}

And who knows. How should we think about the potential impact?

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, so if it's not replaced and it stays the way it is, then we should be fine. Because...

Q - Paul Patterson {BIO 1821718 <GO>}

I mean, it's repealed and they don't -- they repeal and they don't replace it if you're following...

A - Nicholas K. Akins {BIO 15090780 <GO>}

Okay, so Brian...

A - Brian X. Tierney {BIO 15917272 <GO>}

Second part. So that -- we'll be fine in that circumstance, Paul. We already had decoupling in place for residential and small commercial customers. We were already getting recovery of OVEC through 2024 through the regulatory process rather than 2030 and it allowed us to enter into bilateral contracts with customers, but we haven't signed any bilaterals to-date. So we think, we'll be absolutely fine if it's repealed and not replaced, but as Nick said, I think there are opportunities to do it right and replace it with something that's more positive.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah, we've done bilateral contracts just not with that structure, so.

Q - Paul Patterson {BIO 1821718 <GO>}

Okay, great.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Paul Patterson {BIO 1821718 <GO>}

And then, just on the PJM 205 end-of-life transmission planning and filing. I know you guys are protesting that with almost every other transmission company. Do you have any sense as to what the potential impact would be from a shareholder perspective on transmission CapEx or anything else if that 205 filing is accepted by FERC?

A - Brian X. Tierney {BIO 15917272 <GO>}

Paul, we think it'd be pretty minimal to us.

A - Nicholas K. Akins {BIO 15090780 <GO>}

Yeah.

Q - Paul Patterson {BIO 1821718 <GO>}

Okay, good. Awesome. Thanks so much.

A - Brian X. Tierney {BIO 15917272 <GO>}

Thank you.

Operator

Thank you. And at this time, I'm showing no other questions in queue. Please go ahead with any closing remarks.

A - Darcy Reese {BIO 20391516 <GO>}

Thank you for joining us on today's call. As always, the IR team will be available to answer any additional questions you may have. Cynthia, would you please give the replay information?

Operator

Certainly. And ladies and gentlemen, today's conference call will be available for replay after 5:30 p.m. today and going until August 14th at 3.55 p.m. You may the access the AT&T Teleconference replay system by dialing 866-207-1041 and enter in the access code of 7269937. International participants may dial 402-970-0847. Those numbers once again, 866-207-1041 or 402-970-0847 and entering the access code 7269937. That does conclude your conference call for today. Thank you for your participation and for using AT&T Executive TeleConference Service. You may now disconnect.