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Q1 2010 Earnings Call

Event Type▲

Apr. 23, 2010

*Date▲***MANAGEMENT DISCUSSION SECTION**

Operator: Good morning. My name is Christy. I will be your conference operator today.

At this time, I would like to welcome everyone to the Exelon First Quarter Earnings Conference Call. [Operator Instructions] I will now turn the call over to Ms. Stacie Frank, Vice President of Investor Relations. Please go ahead.

Stacie M. Frank, Vice President of Investor Relations

Thank you, Christy. Good morning. Welcome to Exelon's first quarter 2010 earnings review and conference call update. Thank you for joining us today.

We issued our earnings release this morning. If you haven't received it, the release is available on the Exelon website at www.ExelonCorp.com.

Before we begin today's discussion, let me remind you that the earnings release and other matters we will discuss in today's call contain forward-looking statements and estimates that are subject to various risks and uncertainties, as well as adjusted non-GAAP operating earnings. Please refer to today's 8-K or our other filings for a discussion of factors that may cause results to differ from management's projections, forecasts, and expectation, and for a reconciliation of operating to GAAP earnings.

Leading the call today are John Rowe, Exelon's Chairman and Chief Executive Officer, and Matthew Hilzinger, Exelon's Senior Vice President and Chief Financial Officer. They are joined by other members of Exelon's senior management team, who will be available to answer your questions. We have scheduled 60 minutes for this call.

I will now turn the call over to John Rowe, Exelon's CEO.

John W. Rowe, Chairman and Chief Executive Officer

Thank you, Stacie. Good morning, everyone.

In the first quarter, Exelon was able to beat our own expectations. Our results and our confidence in the balance of the year allow us to raise the bottom of our full-year earnings guidance.

As you all know, we are working very hard to manage everything that is within our control, and to keep ourselves positioned for the day when the commodity markets improve. As the economy recovers and capacity in energy markets improve, Exelon will again increase its value. And it will come as either carbon legislation or pollutant regulations impact the oldest and least efficient generating units among our competitors. The timing may be uncertain, but those forces are inescapable.

I will begin with a quick overview of the first quarter. As you've seen in the press release, we recorded operating earnings of \$1 per share, above our guidance range of 85 to \$0.95 per share. We were able to deliver these results through exceptional operating performance and better than expected load at PECO.

Our nuclear fleet achieved a capacity factor of 92.3% – thank you, Chip – while conducting 5 refueling outages. Among these outages was a steam generator replacement at Three Mile Island. The recently completed outage at Quad Cities resulted in plant upgrades that marked 100 cumulative megawatts in added capacity since we announced the program last year.

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ComEd and PECO continue to improve their performance. ComEd recorded its best ever first-quarter results for reliability and frequency of outages. And Denis O'Brien and their team at PECO performed superbly in the face of a series of genuinely extraordinary snowstorms.

As a result of our success in the first quarter, we are revising our full-year guidance from the 3.60 to \$4.00 per share range that we had to 3.70 to \$4.00 per share. In addition to the performance, this reflects the fact that some of our market conditions at Generation are more favorable than our previous forecast. It reflects our continued progress on achieving our O&M targets. And as we told you in January, we now have certainty about our pension expense for the year.

Cash from operations is similarly showing improvement. Matt will walk you through the details, but much of the improvement is associated with the cash benefits of the better-than-expected earnings and with tax planning items.

We are putting cash to work in three different ways. We are maintaining our dividend, we are continuing investing in our nuclear upgrades, and we are – expect to increase our financial flexibility by making a discretionary contribution to our pension fund this year. This will both improve our funded status and reduce our mandatory cash contributions in 2012 and beyond. The price – precise amount will be determined by our Board some time this year, but we anticipate that the contribution will be in the neighborhood of \$500 million.

Before Matt gives you more detail on the financials, I want to update you on what we know about developments in Pennsylvania, Illinois, and Washington.

In Pennsylvania, the headline is obviously PECO's electric and gas distribution rate filings. This is PECO's first delivery rate case filing in 21 years and only the second gas rate case over that period of time. It reflects over 2.5 billion in infrastructure investments in the PECO delivery system, while keeping rate increases very moderate. Denis O'Brien has a chart that shows how the average PECO residential customer can offset the entire increase by installing a programmable thermostat and five compact fluorescent light bulbs.

In addition, PECO has reached an agreement for the \$200 million stimulus award from the Department of Energy to support its Smart Grid and Smart Meter programs.

Finally, Exelon Power has first from PJM that there are some localized transmission improvements that are necessary before the full retirement of Eddystone and Cromby stations. Two of the four units will retire as scheduled in mid-2011, and Generation expects to file for a reliability must run agreement for the other two in the second quarter. It will provide for cost recovery and a return, but will be limited in duration and cover only the periods that the units are needed for system reliability.

Turning to Illinois, ComEd continues to improve both its operating and its financial performance. Frank Clark and Anne Pramaggiore are constantly successful in finding new ways to deliver cost control and revenue improvement. Because of efforts like these, ComEd is on track to achieve an ROE of at least 10% this year. ComEd is preparing for a rate case filing in the second quarter.

Despite a consistent low gas price environment impacting power prices, Ken Cornew and his team are constantly looking for opportunities to reduce down-side risk through longer-term contracts, through the use of options and localized near term transmission upgrade investments that reduce congestion.

Power team has seen the basis spread between Ni-Hub and AEP-Dayton Hub come back in line with historical levels, as we expected and talked to you about back in November. Exelon Generation is planning to invest several millions of dollars in transmission upgrades near the Clinton Station that will lower congestion and improve Clinton's pricing toward the synergy hub.

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Power team is working with the PJM processes to identify other investments in our operating footprint that will improve energy flows and reduce the seam issues with neighboring RTFs.

Now let me say a few words about Washington. I may be the only person in the country willing to say only a few words about Washington.

On the heels of the healthcare debate, the prevailing wisdom is that the odds for passing climate legislation are slim. I don't disagree with that, but there is a great deal of work going on. John Kerry, Lindsey Graham, and Joe Lieberman are working very hard on an economy-wide, sector by sector approach. I anticipate that they will have announcements in this regard next week.

It appears that their proposal will continue to regulate carbon emissions in the utility sector on a market-based, cap-and-trade approach. It also appears that what they are doing will include incentives for low emission sources like nuclear. The outcome remains uncertain, but this looks like it will be a bill that has a much better chance of walking than the previous measures.

Regardless of the outcome of climate legislation, EPA is moving along with its regulatory approaches to using established statutory requirements and regulating a variety of air pollutants. We expect Administrator Jackson and her staff will come out with the first in a long line of regulations in the next few weeks. Coal-fired generation will face very difficult investment decisions over the years ahead.

EPA's effort reinforced for me what has been a guiding principle for Exelon since its creation. That is that the best generation assets are those that run with the lowest emissions profile. And in PJM, Exelon's 17 nuclear reactors are the best of those low emission facilities. We take Exelon 2020 very seriously, and we look at it as a value-added document, as an investment guideline, not simply as a PR or legislated piece.

I would be remiss in talking about Washington without mentioning that Betsy Moler has announced that she will be retiring this summer. Betsy has done a great deal to help build the value of your shares with her work on carbon legislation, with her work on bringing ComEd into PJM, with her tireless advocating for competitive markets, and with her work at FERC.

Betsy is a very special person and cannot be replaced simply. But we have 2 people who I think will fill the hole very nicely. David Brown will lead our DC office, and he has been part of Betsy's team there for – ever since the merger, and for 10 years prior to that, he was with PECO. Joe Dominguez, who has handled legal and governmental affairs for Exelon Generation, will now add the federal regulatory practice to his portfolio. We will continue to have a very good Washington team, but I personally will miss Betsy very much.

And with that, let me turn this over to Matt, who will take you through the financials in more detail.

Matthew F. Hilzinger, Senior Vice President and Chief Financial Officer

Thank you John, and good morning, everyone.

I will start on slides 4 or 5, where I've outlined our key messages for this morning and detailed the first quarter results. We have provided a significant amount of detail regarding our results in the earnings release and the accompanying tables. I'll spend most of my time providing additional color on a few select items in the release and updating you our key highlights for the quarter, and our cash flow outlook for the remainder of the year.

As John mentioned, Exelon delivered operating earnings of \$1.00 per share for the first quarter of 2010, compared to \$1.20 per share in the first quarter of 2009. The first quarter results came in

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above our expected range of 85 to \$0.95 per share, largely driven by better-than-forecast demand at PECO and higher rev net fuel than planned at Exelon Generation. The higher rev net fuel at Generation is principally made up of congestion favorability in Western PJM and the lower MISO ancillary costs.

I'll explain more about what we're seeing with utility load in a few minutes, but let me first turn to Exelon Generation on slide 6. As expected, we saw a decrease at Exelon Generation relative to the first quarter of last year, due to unfavorable market conditions in all regions and lower nuclear volumes. The lower nuclear volumes were driven by more refueling outage days than last year, including 23 days in 2010 related to the outage at Three Mile Island to install steam generators.

Our full-year guidance for 2010 assumes 10 planned refueling outages, which is in line with 2009. However, the outages this year are more heavily weighted to the first part of the year than in 2009: 5 outages were either in process or completed by the end of the first quarter of this year, compared to 3 in the first quarter of 2009. We also have higher nuclear fuel cost quarter-over-quarter, a trend that we expect to see continue as our below market uranium hedges from several years ago are replaced with contracts at levels more representative of our long-term expectations for uranium, which are in the range of 40 to \$60 per pound.

Let me spend a few minutes on slide 7 highlighting what we are seeing in the power markets and hedging activity as we completed this quarter. Based solely on current forwards, market conditions in Exelon Generation's portfolio were challenging. Prices at Ni-Hub and PJM-West Hub decreased throughout the quarter, driven by the decline in natural gas prices. As we have shown in more detail in the appendix of today's slides, our open gross margin reflects this downward movement in prices.

Our hedges have protected much of that move in the near term, as our 2010 hedge to gross margin, for example, is up by 50 million since year-end. We continue to use put options to remain ahead of our 3-year ratable plan in 2011 and 2012. In 2011, about 10% of the hedges are from put options that we purchased to protect against further declines in natural gas and power prices while preserving participation in upward price movement.

As we see power fundamentals improve, we believe that there is still some upside to Midwest power prices from what is reflected in the current forward curve, particularly in on-peak hours. We have seen further compression in the basis differential between NI-Hub and AD Hub to levels that are more in line with historical levels and the last PJM financial transmission rights option.

You'll recall that, mid last year, the spreads between those two trading points implied in the 2012 forwards was about \$13 per megawatt hour. As of the end of the first quarter, and even as of earlier this week, the spread is down to about \$6 per megawatt hour. So even in a declining gas price environment, Ni-Hub prices are holding a little better, relative to AD Hub.

Wind build-out remains challenged given current power prices, and developers continue to have difficulty finding counterparties to execute long-term PPAs. In addition, we are expecting a pick-up in load relative to last year, and all of these factors taken together should have a positive impact on Ni-Hub heat rates.

The capacity component is another key source of Exelon Generation's margin. On the bottom of slide 7, we've shown the breakdown of our total eligible installed capacity by region for the upcoming RPM-based residual capacity auction. As you can see from the pie chart, 50% of our capacity is in the eastern zone of PJM, which received significantly higher prices in the Midwest in the last RPM auction.

We see five drivers that should lead to upside in the clearing prices for the 2013 and 14 auction to be held this May. First, we think there will be some changes in the bidding behavior of auction

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participants, as FERC approved a rule change following the last auction that will allow existing demand response resources to bid in above zero. Second, PJM has increased its demand forecast by about 1.7% compared to the demand assumed in the 2012 and 2013 auction.

Third, First Energy is joining PJM in mid-2011, and they will bring slightly more load than supply. Fourth, the delay associated with the Susquehanna-Roseland transmission line in the East reduces available import capability in the Eastern MAAC by close to 2,000 megawatts. And finally, net CONE, which measures the cost of new build less historical revenues, increased by 15% for RTO and 23% for EMAAC.

In aggregate, these factors should lead to increases in capacity prices relative to the prior auction results. In terms of the timing, initial pricing results are expected to be public on May 14, with the full market monitor report to follow later this summer, which is similar to last year.

Turning to ComEd on slide 8. ComEd improved its earnings quarter-over-quarter, principally due to ComEd's continued cost-reduction work. One other driver in particular that I would like to highlight is the \$0.06 per share of favorability related to the uncollectibles expense rider, which was reflected in our original 2010 earnings guidance. We were able to work constructively with both the legislators and the ICC to develop this rider, which allows ComEd to recover the bad debt amounts not included in base rates. Our first quarter results include the under-collections in 2008 and 2009. And going forward, ComEd will record the true up on a quarterly basis.

As you will see on slide 9, weather-normalized load at ComEd declined 0.8% from the first quarter of 2009 to the first quarter of 2010, which was in line with our expectations. One positive sign is that March was the first month with positive growth we have seen in the ComEd service territory since July of 2008. The residential sector held up especially well, as we added approximately 2,500 customers as of the end of first quarter this year compared to the first quarter of 2009, which is the first time that we've seen positive customer growth since December of 2008.

We continue to track regional unemployment data in Chicago, which is about 10.9% and still higher than the national average. And as a result, we continue to believe that residential load will show flat to very slight improvement for the year.

In ComEd's C&I segments, weather-normal load was down slightly in the quarter, but only by about 200 gigawatt hours over last year. National data like the March Institute for Supply Management survey, which had its highest reading since mid-2004, suggest that manufacturing sector continues to expand, boosted by stronger orders and production. Based on the regional and national trends we're watching and what we're hearing from surveys of our large customers, we think the inflection point in the large C&I class at ComEd is coming around mid-year, and we continue to expect full-year growth in that class of about 1.7%. Across all customer classes, our ComEd forecast for 2010 is unchanged at 0.8% growth for the year.

Moving to slide 10, we've outlined ComEd's \$1 billion revolving credit facility that we closed at the end of March. The transaction shows that the bank market for the investment grade credits is strengthening. We have 22 banks committed in the 3-year facility, and the pricing is lower than any other BBB credit priced in the last year. We continue to track the credit markets so that we can take advantage of attractive terms and conditions for the refinancing of the credit facilities at our other operating companies, which are due to expire in late 2012.

Lastly for ComEd, there are a couple of key events planned for the second quarter. The bids for the Illinois Power Agency procurement are due next week, followed by ICC approval in early May. And ComEd expects to file an electric distribution rate case later in the second quarter.

On slide 11, we have shown you PECO's quarterly earnings drivers. PECO delivered quarterly earnings in line with last year. As expected, PECO's quarterly results include increased revenue net

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fuel related to lower energy pricing to Generation under the PPA provisions, which is fully offset at Exelon Generation. Keep in mind that, because this is the last year before PECO transitions to market, PECO's price for energy paid to Generation under the PPA and the amounts collected for CTC will vary during the year, in order for PECO to complete the collections of its stranded costs.

Separately, weather in the Philadelphia service territory was challenging in first quarter. The region was hit with three snowstorms leading to total accumulation of 79 inches for the 2009 and 2010 winter season, over 300% above normal. And despite the related workload, PECO was just one penny per share unfavorable to the quarter on storm costs.

On slide 12, you can see that PECO's load increased slightly from the first quarter compared to the first quarter of 2009, as PECO is seeing signs of improving demand a bit earlier than originally expected. The large commercial and industrial class is seeing increase load in the steel manufacturing segment, as well as healthcare and educational services. The residential growth appears to be tied to better economic recovery.

Our current forecast for the Philadelphia gross metro product is now 0.6% positive for 2010, as compared to a negative 0.2% at the time we did our original 2010 budget. For the full year, PECO now expects positive growth of 0.3% versus our previous forecast of negative 1.5%, primarily driven by recovery in the residential and large C&I classes.

That revision reflects PECO's actual first-quarter load and general improvement in the gross metro products forecast for the Philadelphia region. The new forecast also incorporates higher usage for customer than we originally anticipated because the PAPUC's approval of energy efficiency programs came a little later than we had originally expected. In turn, the implementation of our energy-efficiency programs was delayed at PECO, resulting in a projected 0.5% increase in total load for the full year.

Turning to slide 13, PECO filed an electric and gas distribution rate cases on March 31, 2010. Highlighting a few items from those filings, both cases are requesting an 11.75% ROE and use a 2010 forward test year, which is conventional in Pennsylvania. The electric case has a rate base of just over 3.2 billion and a requested increase in revenue requirement of 316 million. On the gas side, PECO's request is based on 1.1 billion rate base, with a revenue requirement increase of 44 million. Rate cases are a 9-month process in Pennsylvania, so we anticipate having new rates effective by January 1, 2011.

Slide 14 outlines our latest views on sources and uses of cash. Expected cash from operations for the year has improved by about \$200 million, as we have increased net income over expectations coming from our first quarter results, and second, we are anticipating some favorable cash from option sales and spend strategies of Power team this year.

The cash flows that we've shown also assume an incremental pension contribution this year, as John had mentioned. We expect that contribution to be approximately \$500 million, which will be funded through a combination of increased cash from operations of \$200 million that I just spoke about, plus 170 million from the tax deduction that we get upon making the contribution. And we expect to finance about 150 million with additional debt at ComEd.

Making this additional contribution in 2010 is consistent with our goal of preserving financial flexibility by avoiding significant spikes in future required contributions under our residuals. The Pension Protection Act of 2006 carries with it a requirement to fund the pension within approximately 7 years. Given those requirements, which we view as being very similar to debt service, we see the pension contribution as the best way to meet our financial obligations in a tax-effective manner and deliver long-term value.

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Lastly, I would like to point out that our expected ending cash position has increased from 175 million that we showed you in January to \$500 million now. That increase is simply due to the timing of tax payments for the year, about 375 million of which are being deferred to 2011. That amount is showing up in 2010 ending cash, but it must be paid in 2011.

As we look ahead, we expect second quarter operating earnings in the range of 80 to \$0.90 per share. Our second quarter range reflects lower realized prices in Exelon Generation given market conditions as well as increased nuclear fuel costs similar to the first quarter. That's being offset with some favorability related to our latest load growth expectations, continued progress on O&M targets for the year, and higher RPM capacity prices, which will become effective on June 1 of this year. We will continue to give specific quarterly guidance one quarter at the time.

We are very pleased with how the year is shaping up so far, and we are pleased to have raised the bottom of our guidance range to reflect our first quarter results and our best expectations for how the rest of the year will come in.

And with that, I will turn the call back to Stacie.

Stacie M. Frank, Vice President of Investor Relations

Christy, we are now ready to take questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Daniel Eggers with Credit Suisse.

<Q – Dan Eggers>: Hey, good morning.

<A>: Good morning, Dan.

<Q – Dan Eggers>: First question on the guidance update, as it relates to kind of the generation outlook.

How much of that is sustainable of that up-tick this year? I mean, pricing isn't that fantastic. So do you guys think you are going to retain that extra 10 to \$0.15 going forward from an operational improvement perspective?

<A – Matthew Hilzinger>: I will jump in and – this is Matt Hilzinger – and then Ken can comment if he'd like. There's a couple of things that really drove our first quarter above our expectations that I had mentioned. One was congestion in the Midwest, and the second was MISO ancillary cost. And the second was higher load at PECO.

PECO is going to get probably \$0.02 from their increase in load for the full year. And I would expect that to translate to somewhere around \$0.03 for the generation company. And so, we factored that into kind of our full-year guidance. And that's really part of the reason that we brought our bottom up.

And then the third thing, Dan, you probably recall that in January, we raised or changed our guidance around pension cost. The discount rate in came a little higher at year-end than we had originally planned and what we had said at EEI. And so we are going to see about \$0.05 better in pension cost, relative to actual, to what we had said at EEI.

And so both – all three of those things, I think, factored into how we looked at our guidance. And our O&M is on line. I mean, we expect to hit targets there. So with that, I think we're in pretty good shape as we finish out the year.

<Q – Dan Eggers>: Okay. And I guess one more question, as we kind of look at the RPM auction coming up.

Obviously, the past 2 auctions, Eddystone and Cromby, didn't get bid or didn't clear, because the energy value wasn't high enough, with tough forward curves today. Do you have other assets you anticipate setting a notably higher standard for market clearing? And Ken, if you look out into the auction cycle, there are 9,000 megawatts that didn't clear last auction. Do you guys have a thought on how many more units wouldn't clear, given how tough the forwards are today?

<A – Kenneth Cornew>: Yeah, Dan, I think it's largely going to be an element of what the bidding behavior is of the generation going forward in these auctions. I think, clearly, what the market monitor released saying that a substantial amount of generation didn't clear in past auctions is likely to continue in future auctions unless prices increase.

Now, Matt highlighted and you are all looking at what are the price drivers that are going to – or are the auction drivers that are going to push prices up? And we believe they will. The question really becomes what the bidding behavior of the generators and the demand response will be versus the past.

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And I would expect to see, over time, that generators are going to – these generators that are older and not clearing are going to have a more challenging time continuing to exist and offer their capacity in the market. I think that will happen probably over the next several years, just not instantaneously this year.

<Q – Dan Eggers>: Do you guys have other generation assets that you'd put in that vulnerable category, beyond Eddystone and Cromby?

<A – Kenneth Cornew>: We've looked at our generation, obviously. We made the decisions around those we felt were challenged, and those are the ones at this point, Dan.

<Q – Dan Eggers>: Okay. Thank you.

Operator: Thank you. Your next question comes from the line of Hugh Wynne with Sanford Bernstein.

<Q – Hugh Wynne>: Good morning, and – hi. Congratulations on a good quarter.

I was going to ask you to elaborate a little bit on your comments, John, regarding the EPA's regulations away from CO2 to limit emissions of SO2 and mercury. It strikes me that your fleet in Northern Illinois might benefit materially from some of the older coal-fired units in that state being forced to go offline rather than incur the cost of mercury and acid gas emissions controls. And I was hoping I might get some insight from you as to what your expectations are regarding those regulations, their impact, and the potential implications for your revenues?

<A – John Rowe>: Well, we think exactly what you do on that subject. I think there are at least 3 or 4 units in Northern Illinois that are owned by others for which incremental investment to comply with tighter standards would be a very vexing thing indeed.

Now, obviously, we don't have and aren't allowed to have any peculiar insights into what the owners of those units may be doing, but we intend to be ready, when those decisions have to be made.

I think you have your finger on it exactly. I don't think we're going to see EPA using CO2 regulatory powers in a Draconian fashion. My guess is that they believe that that would create an unsustainable amount of congressional kickback.

But EPA has rule-makings on coal ash to come out soon. It has what is call the CAIR, C-A-I-R, regulations on SOx and NOx. It has, as you suggested, the hazardous pollutant regulation on mercury. I think somewhere in that chart that people call train wreck, there is also new particulate regulation. And it's just hard for me to see how each and every one of these won't impose a new investment requirement and additional cost requirement on all of the older and smaller coal-fired units, especially some that exist in Northern Illinois.

As we look at it, something we do know, simply from industry discussion, is that a number of utilities have tried to approach EPA about whether there is some way to put all of their plans for their units in a bubble, and get credit for shutting down some against the operating requirements for the bigger, better ones. And I think EPA told them it doesn't quite work that way because of the lawsuit that they brought themselves. EPA feels that it has to enforce each of these statutory requirements on its own unique terms. And that's going to place some real burdens on some of these plants.

So I wish it had the sort of predictability that good CO2 legislation would have. But I think it's in some ways even more dramatic in its long-term outcome.

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<Q – Hugh Wynne>: Do you see the impact primarily on the energy prices, John, or do you think that there will be a material impact also on capacity prices over time?

<A – John Rowe>: I would think capacity perhaps even more than energy, but I'd like Ken Cornew to pick that one up. Ken?

<A – Kenneth Cornew>: Yes, Hugh, I think it's both. To the extent there is more cap and trade in these elements, those types of costs get into the dispatch of the generators, and that will impact the energy market.

To the extent it's investment, obviously, and capital, that's going to look large in a 5-year or 6-year future timeframe, and that is going to have to make its way into the cost for generators to bid into RPM. So I think it's definitely some of each.

<Q – Hugh Wynne>: Great. Thank you very much.

Operator: Your next question comes from the line of Jonathan Arnold with Deutsche Bank.

<A – John Rowe>: Good morning, Jonathan.

<Q – Jonathan Arnold>: Good morning. I wanted to ask a question about your hedging during the quarter.

It seems that – well, within the broad remit of the ratable plan, you did hedge somewhat more than you could have done. And you also made the statement in the beginning, John, that you kind of remain optimistic about future prices. Is it reasonable to assume you just don't feel that optimistic in the 2012 timeframe?

And then I wanted to also – is there an element here of potential change to hedging around the new regulations in financial reform, et cetera, that – is there anything you are doing today you feel concerned that you might not be out to do in the same way?

<A – John Rowe>: I'll let Ken answer most of that, but just let me say, we know all of you are concerned about 2012 prices. So are we.

We can't predict just when some mix of tighter capacity, higher gas prices, higher coal prices, and some carbon penalty really begins to have an effect. We're very sure it will be there, but whether it's 12 or 14, we have no better way to know than you do. So our approach to this is fundamentally manage our hedging strategy in accordance with what we see, manage the company so that we take our long-term forecasts and deliver real results that beat those forecasts.

And it's kind of funny. In my – now many, many years – the period from, say, '05 to '08, is the only time I've ever had good long-term 5-year forecasts, and those turned out to be wrong. Most of my experience has been that you have bad long-term forecasts, and you work like hell to make the reality better than what the machine says, and often you succeed.

So that's how we deal with this commodity trough. But with that, I'd better let Ken answer the greater detail of your question.

<A – Kenneth Cornew>: Yeah, Jonathan. Obviously, when we talked about this the last quarter, we came into this quarter above ratable. And we talked about the use of options and some of the uncertainties that we were looking at regarding economic recovery and its impact on gas and power demand.

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We've started ahead of ratable in the Midwest obviously with that ComEd swap, and we've remained ahead of it since the 3-year plan has been instituted. We did increase our mid-Atlantic activity of underlying sales to essentially catch up to ratable with the PECO contract rolling off at the end of 2010. We did have some reduction in expected generation, and we did have some higher effect in this in hedging from our put options. So where we are is we're at ratable with our underlying position, and we're ahead of ratable with the put option strategy.

We do that because we do think there is upside in the markets, particularly when I look at heat rates. I'm still seeing spot heat rates disconnected from forward heat rates. You talk about the AEP-Dayton Ni-Hub spreads, and how they've come from a \$13 level in the forwards last summer, all the way back to the \$6 level now.

John mentioned and we talked about how we're working to improve in areas of the transmission grid to make sure we can deliver our power to the broadest markets. We've seen really some good support in Ni-Hub off-peak prices in the quarter and some good support in the forwards, also.

Matt mentioned wind build-out. The wind build-out is obviously slowing down in our minds, and it's tough to get a long-term contract to build a wind facility in this price environment.

So we do believe there is upside in Ni-Hub heat rates. We do believe that a lot of the environmental impacts are going to happen outside this hedging window. And where the uncertainty really comes in is around how quickly the economy is going to recover, and what that does to gas and power demand.

<A – Kenneth Cornew>: And your second part of your question, I think, was are we doing anything differently because of potential CFTC regulation. And the answer to that is simply no.

We continue to focus on our hedging program, utilizing all the channels we've talked about in the past. Load following, standard products at different basis hubs, participating in the retail business competitively, and all kinds of structured transaction opportunities that we look at from time to time.

<Q – Jonathan Arnold>: And could you just comment more -

<A – Elizabeth Moler>: This is Betsy Moler. If I could comment on the derivatives legislation, which was also part of the question. We are cautiously optimistic that the ultimate definition of who gets an end-user exemption in the derivatives legislation will provide us the ability to avoid the CFTC clearing requirements. The Senate Agriculture Committee approved a version of the bill earlier this week that provides such an exemption. While the language isn't ideal, we're certainly making progress there, and we're hoping that we'll be covered when the bill – when and if the bill finally becomes public law.

<Q – Jonathan Arnold>: Can I just ask a clarifying – would that allow you to continue to – would that language allow you to continue to hedge – it sounds like you're hedging commodity exposure, but trying to keep some of the heat rate upside, which obviously requires the use of options and the like. Would that also fall under such an exemption?

<A – Elizabeth Moler>: We hope that the ultimate definition will, but it's really a work in progress right now.

<Q – Jonathan Arnold>: All right. Thanks very much.

<A – John Rowe>: Thank you.

Operator: Thank you. Your next question comes from the line of Michael Lapides with Goldman Sachs and Company.

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<Q – Michael Lapedes>: Hi. Really two questions that are separate from each other. One on Generation, one on the regulated side of the business.

On the Generation side, are there any balance sheet reasons why you implement kind of such a long range – meaning a 3-year prorated hedging program – or is it driven largely by something else?

I mean my gut is that a nuclear generator – you're always going to run, you're always going to be in the money. Why hedge, if the fundamental view is that power prices are low for kind of that third year? Why not leave a large chunk of that third year open, rather than even having 50% of it hedged. That's the first question.

The second question, just curious for insights, outlook on State of Illinois utility regulation, in terms of kind of going into the ComEd rate case?

<A – John Rowe>: Okay. Let me start with the first one, and Matt and Ken will help me here.

I do not think there is a real balance sheet reason for the ratable 3-year hedging, but Matt and Ken may have a thought that I don't. Obviously, things like supporting the dividend are a reason to have a hedging policy.

We have sat back from time to time and said, should we do what Exxon does and simply say our fundamental business is too big to hedge? But we have thought the 3-year policy allowed us to bring some stability to earnings and cash flows that we wouldn't have otherwise. And as I think you gathered from an earlier question that Ken answered, he kind of thinks that he is able to get some forward deals now in '12 that are just a little better than the spots might be when we get out there.

There is an anomaly in electricity in that forward markets don't go very far out. And long-term contracts by people with load-serving responsibility tend to be at higher prices than the sum of the intervening spot markets. And I think that also supports what Ken is doing.

But now, Matt and Ken, tell me what I missed. Tell him what I missed.

<A>: I would add to that, John, that the hedging is there to really protect and help reinforce our investment grade rating, and provide some stability over the course of – call it 18 months to 36 months in terms of cash flows. So if a plant goes down, operational risk, that we were covered from that.

And that is really kind of the key reasons why we hedge, is to protect on the operational side, protect our investment grade rating. And then thirdly, it helps in terms to just access to capital. There's a lot of things that we do from a commercial standpoint that require investment grade ratings that we think are important.

So those 3 things I think are the real fundamental underpinnings of why we hedge in the way that we do.

<A – John Rowe>: Could we switch now? Frank, would you pick up his question about Illinois?

<A – Frank Clark>: I'll start, and our President can also add some perspective. As we have announced, it is our intent to file a rate case for ComEd near the backend of the second quarter of this year. That is still our plan.

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The regulatory climate in Illinois is about the same as it was before. We have a new Chairman of the Commerce Commission, Chairman Flores, who has not been confirmed by the Illinois Senate, and don't know that he will be confirmed before the Senate ends its session. It's an unknown.

I think that the regulatory climate is essentially the same as it was before, when we had Chairman Box. I think that our expectation is that we will be treated fairly when we file our rate case.

The Illinois regulatory climate is directly related to the Illinois political climate, which is – at it has been for the last decade – in an interesting state. And Governor Quinn is trailing in the polls to Senator Brady, a Republican who may actually succeed. If he does, we will probably get a different chairman, who would be in that seat, probably I would expect sometime early next year.

So there are uncertainties, but the overall balance in the regulatory climate, in my judgment, remains essentially the same. Anne?

<A – Anne Pramaggiore>: Yes, Frank, the only thing I would add is we understand the regulatory climate in Illinois pretty well, and we work very hard to put ourselves in the best position possible coming into these rate cases.

We have worked – we have a history now of working very constructively with the staff. In the last rate case, we worked constructively with stakeholders on the smart grid project that's been going on over the last year and a half. We took a lot of cost out of the business last year. That's well known at the Commission. And they also recognize that we work very hard to stay out last year, and extend the time for the next rate case.

So I think that's all recognized, and should put us in a reasonably decent position going in to this case.

<Q – Michael Lapidès>: Got it. And just address, what was your last either rolling 12 months or 2009 earned ROE at ComEd?

<A – Anne Pramaggiore>: 8.6.

<A – John Rowe>: 8.6 was the answer they gave.

<Q – Michael Lapidès>: Okay. Thank you, guys. Much appreciated.

<A – John Rowe>: Thank you.

<A – Stacie Frank>: Christy, we have time for one more question before turning the call back to John to conclude.

Operator: Thank you. Your final question comes from the line of Paul Ridzon with KeyBanc.

<Q – Paul Ridzon>: When we look at to your hedge update – looking at '12, for instance, you're basically about 50% hedged. How much of that is through puts, and therefore the upside is still preserved?

<A – Matthew Hilzinger>: Yes. It's a little more than 5% of that through puts.

<Q – Paul Ridzon>: So, 5% of the 50%?

<A – Matthew Hilzinger>: Yeah.

<Q – Paul Ridzon>: About 2.5%?

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<A – Matthew Hilzinger>: Yes. Oh, no. 5% – it's 5% of the nominal 50%. So we're – with underlying, it would be something like 43 to 45% hedged. And with the puts added, it's more like 48 to 51. Is that clear?

<Q – Paul Ridzon>: Yes. And you started kind of using the put strategy more recently?

<A – Matthew Hilzinger>: We actually employed the put strategy in prior quarters for 2012. We started the put strategy earlier on in our ratable hedging program. So in '09, we started doing it.

<Q – Paul Ridzon>: Thank you very much.

Operator: Thank you. I'll now turn it over for closing remarks.

John W. Rowe, Chairman and Chief Executive Officer

Thank you all very much.

Stacie and her team will continue to answer your questions. And I think she and her predecessor Karie Anderson have done a great job trying to improve the quality of the materials we put out in public, so we get to a lot of your questions before the meeting. But we'll keep working on as much clarity as we can provide.

Simply put, Exelon is 70 to 75% a commodity-driven business and 25 to 30% a regulatory-driven business. And the commodity business was a hell of a lot of fun two years ago. It's a lot harder work right now.

As our results for the first quarter show, we're able to beat our own model sometimes by hard work, and we'll continue to try very hard to do that. We'll try to give you a really good year this year. And we will keep working on the questions you all have about 2012. We have a long time ahead of us before 2012 comes. I'm confident we'll find some good things to do in that intervening period.

Thanks a lot for your patience, and life at Exelon will be fine again one of these days.

Stacie M. Frank, Vice President of Investor Relations

Thank you. That concludes our call.

Operator: Thank you. This concludes today's conference call. You may now disconnect.

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