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+++ presentation

Operator^ Good day, ladies and gentlemen, and welcome to the Black Hills Corporation Second Quarter 2022 Earnings Conference Call. My name is Liz, and I will be your coordinator for today. (Operator Instructions) As a reminder, this conference is being recorded for replay purposes. I would now like to turn the presentation over to Mr. Jerome Nichols, Director of Investor Relations of Black Hills Corporation. Please proceed, sir.

Jerome E. Nichols^ Thank you. Good morning, everyone. Welcome to Black Hills Corporation's Second Quarter 2022 Earnings Conference Call. You can find our earnings release and materials for our call this morning at our website at www.blackhillscorp.com under the Investor Relations heading.

Leading our quarterly earnings discussion today are Linn Evans, President and Chief Executive Officer; and Rich Kinzley, Senior Vice President and Chief Financial Officer. During our earnings discussion today, some of the comments we make may contain forward-looking statements as defined by the Securities and Exchange Commission, and there are a number of uncertainties inherent in such comments.

Although we believe that our expectations and beliefs are based on reasonable assumptions, actual results may differ materially. We direct you to our earnings release, Slide 2 of the investor presentation on our website and our most recent Form 10-K and Form 10-Q filed with the Securities and Exchange Commission, for a list of some of the factors that could cause future results to differ materially from our expectations.

I will now turn the call over to Linden Evans.

Linden R. Evans^ Thank you, Jerome. Hello, everyone, and thank you for joining us.

I'll start on Slide 4 of our investor presentation. During the second quarter, we delivered solid financial results and advanced our strategic initiatives. I especially note our progress with our regulatory initiatives and our electric resource planning, and we reaffirmed our 2022 earnings guidance yesterday.

Our success starts with our dedicated team and their commitment to serving our customers with excellence. I'd like to express how proud I am of our team for delivering the high level of operational performance that our customers depend upon every day.

Safety and reliability are critical as we journey through the nation's clean energy transition. The July heat wave recently demonstrated once again the critical need for reliable and dispatchable capacity and the importance of a responsible mix of resources.

Once again, for the ninth consecutive summer, our Wyoming Electric System marked a new all-time demand peak and our South Dakota Electric System also surpassed its all-time peak from last summer, reflecting the ongoing customer growth in our service territories.

Our industry-leading generation and system availability made it possible for us to keep homes safe and keep businesses operating without any restrictions or forced outages. Our vertically integrated model with nearly 1,500 megawatts of owned generation allows us to serve our customers safely, reliably and cost effectively during these volatile energy markets.

We were also successful with another innovative customer solution during the quarter. Our team completed its first agreement for service under our blockchain tariff in Wyoming with a well-established crypto miner that is investing in long-term operations in Cheyenne. We anticipate our customers will begin taking delivery of up to 45 megawatts of energy by year-end with an option to expand service up to 75 megawatts.

The energy for this customer will be sourced through the energy markets and delivered through our reliable infrastructure, which will benefit our other Cheyenne utility customers.

On Slides 5 and 6, we've outlined our progress with our regulatory initiatives. I'm pleased that our Arkansas gas rate review continues to advance on schedule with a hearing before the Arkansas Commission later this month. Our request seeks to implement new rates in the fourth quarter and implement an enhanced system safety, integrity and reliability rider.

On June 1, we filed a rate review for Wyoming Electric. We're requesting new rates in the first quarter of 2023 to recover the $250 million of investments we have made in the Cheyenne region since our last rate review 8 years ago in 2014.

We also made progress with our winter storm Uri cost recovery during the quarter. Thus far, we've recovered more than 1/4 of the incremental costs we incurred to serve customers during storm Uri. In June, we received final approval for our recovery plan in Arkansas, and we're waiting for a final decision in Wyoming where we started collecting interim rates last September.

We also filed for approval of our voluntary renewable natural gas and carbon offset programs in Colorado and Kansas. The proposed tariff will allow business and residential customers to opt into the program. Looking forward, we're also preparing to file a rate review later this year for Rocky Mountain Natural Gas, our intrastate natural gas pipeline in Colorado.

The last 2 items to cover on Slide 5 are related to our long-term transmission and electric resource planning for Colorado, South Dakota and Wyoming. Our theme for 2022 is powering a better future, a recognition to the ongoing clean energy transition. We're optimistic about our generation and transmission opportunities as part of this transition and our plan to expand our energy delivery systems to meet growing customer demand while maintaining resiliency and reliability and developing a smarter ~~drill~~grid.

We've laid out a clear path forward for our infrastructure across our electric utilities. in total,~~.~~ We plan to add 600 megawatts of renewable resources in battery storage and 260 miles of electric transmission as part of our Ready Wyoming initiatives.

Slide 7 summarizes our clean energy plan for our electric utility in Colorado. The plan laid out a path to a 90% reduction in greenhouse gas emissions intensity by 2030 from a 2005 baseline. Our proposed plan to achieve this goal through the addition of approximately 400 megawatts of renewable wind and solar resources and 50 megawatts of battery storage between 2025 and 2030.

We already closed our only remaining coal plant in Colorado back in 2015, and these new clean energy additions would result in almost 80% of our Colorado customers electricity coming from carbon-free resources. Importantly, the reliability of our system is supported by the dispatchable Colorado airport generating station.

We expect to initiate the competitive bidding processes by mid-2023 for these new resources and Colorado legislation provides up to 50% utility ownership of these additions.

Slide 8 summarizes our resource plan that we filed last year for our jointly-operated electric system in South Dakota and Wyoming. As the slide indicates, our proposed plan includes the addition of 100 megawatts of renewable resources and potentially 20 megawatts of battery storage. We're preparing for the next steps that will likely include a competitive bidding process in which we will participate.

And Slide 9 summarizes our Ready Wyoming transmission project and the benefits we expected to provide for customers for the state of Wyoming and for our shareholders. The project continues to advance through the regulatory process on pace with our expectations.

Moving to Slide 10. We're excited about the tangible progress we've already delivered on our emissions reduction goals and other ESG goals. To date, we've already reduced our emissions intensity by more than 1/3 since 2005. Later this month, we will publish our updated sustainability report which will provide detail on this and many other key ESG factors.

We'll also provide key updates for other ESG disclosures, including SASB, the AGA, EEI templates and the national grid initiatives. Notably, we will, for the first time, published TCFD disclosures. We're excited about our progress for both our electric and gas businesses and delivering a cleaner more efficient energy future for our customers and our communities. So please review our reports later this month to find out more.

Slide 11 summarizes our long-term growth plan. We're focused on growing long-term value for customers and shareholders through our customer-focused capital investment program, developing incremental capital projects such as those that could result from our electric resource planning and executing on other opportunities to grow our earnings stream. Those other opportunities include investments to support and attract new customers such as our newly announced blockchain customer.

We are also improving our effectiveness and efficiency as a team, as I described previously on our Energy Forward initiative. We're cultivating a mindset to identify and think more holistically about how we can better serve our customers every day.

We continue to deliver progress on this plan during the first half of 2022 and look forward to developing these opportunities for the future. That completes my comments, and I'll now turn it over to Rich for the financial update. Rich?

Richard W. Kinzley^ Thanks, Linn, and good morning, everyone.

I'll start on Slide 13, which shows our second quarter EPS and segment operating income for 2022 compared to 2021. EPS was $0.52 compared to $0.40 in Q1 2021. And year-to-date, we delivered $2.33 compared to $1.93 in the first half of 2021. That's an increase of 21%.

We experienced a typical shorter period for both our electric and gas businesses with relatively normal weather. Earnings were primarily driven by new rates and riders and a onetime benefit related to winter store nearing cost recovery at our gas utilities, higher operating expenses tempered results.

Slide 14 illustrates the detailed drivers of change in net income year-over-year for the second quarter. All amounts are after tax and more detail is available in our earnings release distributed yesterday and in our 10-Q to be filed later today.

Margins improved due to new rates at our gas utilities and recovery for rider eligible investments across both our electric and gas utilities. A significant driver in the second quarter was a onetime $0.12 EPS benefit for a true-up of carrying costs related to winter storm Uri.

Weather was comparable to the prior year for both the quarter and the first half of the year. For the second quarter in 2021 and 2022, weather provided $0.01 per share benefit versus normal.

Year-to-date through June this year, weather benefited earnings by $0.07 compared to normal versus $0.08 of weather benefit in the first half of 2021. We recognized a negative mark-to-market adjustment of $0.03 of EPS in Q2 2022 on energy contracts which was comparable to the Q2 2021 negative impact of $0.02.

Please see Page 31 in the appendix for detail on the quarterly impacts of weather, mark-to-market adjustments and Winter Storm Uri. For the quarter, O&M was higher mainly due to inflationary impacts driven by higher outside services, noncompeting costs and vehicle fuel costs.

DD&A increased in our capital investment program and interest expense for the quarter increased due to higher short-term interest rates. Other income was higher due to reduced expense related to our nonqualified benefit plans driven by stock market performance.

Taxes were favorable due to a onetime benefit from a state rate change and higher PTCs from increased wind production and a current year federal inflation adjustment to the PTC rate. These were partially offset by prior year benefits from TCJA-related bill credits and pull-through benefits related to repairs and maintenance.

Slide 15 shows our financial position towards capital structure, credit ratings and financial flexibility. We have a manageable debt maturity profile, and we're committed to maintaining our solid investment-grade credit ratings. Our debt to total capitalization ratio improved to 60.7%, down from 62% at year-end, thanks to strong cash flows and recovery of storm Uri costs in the first half of 2022.

We expect to achieve our target capital structure of mid-50s by late 2023 or early 2024 as our business generates strong cash flows and we recover storm costs, repay debt and execute on our aftermarket equity offering program.

Now moving to our dividend on Slide 16. We've increased our dividend an average of 6.4% annually over the last 5 years. Our 2021 dividend represented 51 consecutive years of dividend increases, one of the longest track records in our industry and a record we're quite proud of. Looking forward, we anticipate increasing our dividend by more than 5% annual to 2026 as we maintain our 50% to 60% payout target.

In closing, our overall financial outlook is listed on Slide 17, which is consistent with our prior disclosures. We continue to anticipate 2022 earnings in the range of $3.95 to $4.15 per share.

To date, we've been able to largely mitigate the impact of rising interest rates, inflation and supply chain constraints on our financial results. We remain confident in our long-term growth plan while recognizing that these factors pose a challenge for the second half of this year and 2023.

Regarding expectations for our capital plan, we've noted previously that certain investments due mainly to inflation were deferred to maintain our 2022 and 2023 capital investment in the neighborhood of $600 million to enhance our liquidity and balance sheet.

As a reminder, we expect to refresh our 5-year base capital plan and initiate next year's guidance when we release our third quarter earnings report in early November. So between Linn and my comments, I think we've covered the information shown on this slide.

And with that, we'll take questions. As you can likely tell, Linn and I are in different locations today. So please do bear with us as we answer your questions.

+++ q-and-a

Operator^ (Operator Instructions) Our first question comes from Paul Zimbardo with Bank of America.

Paul Andrew Zimbardo^ I just want to kick it off with kind of a cleanup. How should we think about that you call it the onetime winter storm Uri carrying cost true-up? Was that contemplated in the original 2022 guidance? And if not, are there other kind of offsets we should be thinking about?

Richard W. Kinzley^ That was not contemplated in our initial guidance, Paul. We did contemplate some carrying costs, but this was a true-up based on some outcomes in the different states during the second quarter.

Paul Andrew Zimbardo^ Okay. Are there other kind of unrelated offsets in the year? Or should we just think about it as tracking well in the year?

Richard W. Kinzley^ I think you're pointing toward our full guidance for the year, I take it, right? And I would just suggest we'll get 6 months left to go. We're managing through the inflation and the things that are coming at us from a headwind perspective. We certainly feel very comfortable with our guidance range and are sticking with it.

Paul Andrew Zimbardo^ Okay. Crystal clear. And then changing topics a little bit briefly, just how to think about the balance sheet as it relates to cash taxes?

I know minimum tax is super topical, but I don't think you would trigger the provisions given your pretax income, but just kind of holistically thinking about like the cash tax rate and what you expect going forward?

Richard W. Kinzley^ Yes, this quarter had -- well, our cash tax rate is going to run in that 10% to 12% if you're asking for post 2022. Is that where you're going?

Paul Andrew Zimbardo^ Correct. Yes. Okay. Because I think it's been a little bit lower in the past few years.

Richard W. Kinzley^ Yes. And as our pretax income continues to increase the PTC, unless we add some more renewable projects or some other things, the effective tax rate should increase a bit as we move forward.

Paul Andrew Zimbardo^ Okay. That makes sense.

Linden R. Evans^ Thanks, Paul. This is Linn. I'll just add real briefly just how proud we are of the team, the regulatory team and how well they've done with storm Uri recovery, just outstanding success there and really demonstrating our relationships with our commission. So I want to thank that team and acknowledge them. So thanks for your questions, Paul.

Operator^ Our next question comes from Andrew Weisel with Scotiabank.

Andrew Marc Weisel^ If I can take one more shot at that guidance question. Are you suggesting that you're pointing towards the high end, thanks to the gain, the low end because of those warnings or somewhere in between? Or is it simply no comment?

Richard W. Kinzley^ Linn, feel free to comment on top of me, but what I would say is we're not guiding toward either end of the range. We're sticking with the range. We got 6 months to go and weather, various other things can impact, Andrew. So we're sticking with that range.

Linden R. Evans^ Yes. I think Rich nailed it. We're sticking with our range. We got lots of opportunities through the year, both pro and con. We'll see how the weather impacts us, but we're confident in the guidance range we put out, and I'm very pleased with how our team has responded to inflationary pressures and continue to perform from an operations perspective, and we're very proud of that. So we're going to stick with our guidance for the remainder of this year.

Andrew Marc Weisel^ Okay. Thanks for clarifying. I just wasn't sure if you were trying to suggest one way or the other of the messaging.

My next question is about new renewables and storage. What's your latest expectation about how much of that you'll be able to own in rate base versus buying the output under PPA? I know that in Colorado, at least 50% is the ceiling. But how are you thinking about your competitive position?

Linden R. Evans^ Well, we're always speaking to -- and we think that's what's best for customer rate-based assets where they get the advantage of the depreciation, Andrew. And in my 20-plus years in this business and with this company, I've seen very few PPAs that really worked out well for the customer in the long term.

So we believe taking the customers' perspective, ownership is the best thing. Now of course, we'll see how that works through the regulatory environment on the regulatory process for Wyoming and South Dakota, very likely to put out RFPs and we will bid into those as aggressively as we can.

And as you just mentioned, Andrew, in your question, in Colorado, the legislation indicates we can have up to 50% or own up to 50% of that generation on behalf of our customers, which we think is very positive.

If we look at the Inflation Reduction Act, we've had a few days of that now in terms of our review, so we're still learning that, leaning on our trade associations and our own team to review that, but that tax credit transferability strikes us as being something that could be, if the bill passes, quite positive, allow us to have a much more competitive position as we get into those RFPs going forward.

So we're watching that closely. And we'll see if that gets passed, but we were always looking at lots of different opportunities, whether they be bill transfers, tax equity partnerships and those kinds of things.

So we're always being creative in how we look at them. And we have a team that's very focused on that, owning as much as we think we can, again, primarily because we think that's the right thing to do for customers in the long term.

Andrew Marc Weisel^ One last follow up, if I can. On blockchain, I know that the tariff is interruptible. Can you kind of explain the strategy behind that? Is the hope that cryptocurrency mining might become enough of a source of demand over time that they could be something of a lever to pull for reliability, for example, on peak demand days or extreme weather events?

Linden R. Evans^ Well, they are interruptible [for] customers for a couple of different reasons. One, we want to make sure that our current customers are protected in terms of those peak days, et cetera. The arrangements that we have entered into at the blockchain miner is that we go out to the market of paying that energy for them and then they pay us a fee, if you will.

And we have the opportunity on an hour-by-hour, day-by-day basis to determine whether they want to take the energy or not. So it really provides us a great opportunity to add income to the organization without capital expense.

These entities that we are contracted with, they put the capital upfront, build the necessary infrastructure for us to serve them. They are creditworthy customers, and we're excited to serve them and provides us a great upside for the organization through the arrangements that we've put in place with them. Rich, may have something to add to that?

Richard W. Kinzley^ The one other thing maybe to add to that is it also benefits our customers in Wyoming.

Operator^ Our next question comes from Brian Russo with Sidoti.

Brian J. Russo^ Just to clarify the Colorado legislation that allows the utility to own up to 50%. Are you still subject to the competitive RFP? Meaning, whatever you -- will the utility have to bid in generation that's deemed least costs, least risk? Or could that be bypassed with maybe some -- with this legislation?

Linden R. Evans^ Good question, Brian. Thank you. We're still learning what would happen there. We'll watch what the commission determines that we should do. We're about 6 to 9 months behind itself. We're watching their docket quite closely as they go through their plan.

We believe likely, yes, we'll probably have to put some kind of bid forward with the understanding that the legislation indicates that the price needs to be comparable to the bids that we will receive. So more to come with respect to that.

We are anticipating that we will own up to 50% of the approved generation. We're excited to be able to have that opportunity, but we'll see how the regulatory environment and the construct evolves over time.

Brian J. Russo^ Okay. Got it. And then can you just remind us how much equity do you plan on issuing under the ATM in '22 and 2023? And does the cash collections from winter storm Uri that you've outlined, I believe, page 6, combined with some -- it looks like non-project related earnings drivers that could help further support cash flow. Would that lessen your equity needs going forward, all else equal?

Richard W. Kinzley^ Yes. Well, our guidance indicates $100 million to $120 million this year, so we've got $80 million to $100 million. We think we can comfortably do that in the second half of the year. We haven't put specific numbers out for next year, but you probably should think about the same ZIP code.

And then as to your Uri comment, we've been -- that's gone along very well. Collections have come along. We're right on track with what we thought we would and that's certainly helping our metrics as well. And then you mentioned additional drivers that are helpful, so that will help us shape what our formal 2023 guidance or when would come out with third quarter earnings and give our guidance for next year.

Operator^ (Operator Instructions) Our next question comes from Brandon Lee with Mizuho.

Wayne Lee^ Most of my questions have been asked. Just a quick one. Are you seeing any slowdown in customer growth in some of the service territories that really benefited from a population migration during the pandemic, maybe the Rapid city area or even the Arkansas area.

Just given the high home price appreciation in those areas, have you seen any sort of slowdown?

Linden R. Evans^ Great question, Brandon. Thanks for raising that. The answer to that is no, we have not seen any slowdown. In fact, we're continuing to experience strong in migration both -- in all 3 that you mentioned Northwest Arkansas, front range of Colorado and then now the Black Hills has been added to that list over the last couple of years.

So our customer migration is very strong. We're seeing really strong recovery in our commercial and industrial loads back to more than pre-pandemic levels.

Residential, you'll see in our 10-Q is just a little bit, but I think that's because people are going back to work, which is good for our local economies. So the answer to your question is very strong growth continuing in our regions. And again, you'll see that in our 10-Q that we put out today.

Operator^ With no further questions, I will return the call back to Linn Evans for closing remarks.

Linden R. Evans^ Well, thank you very much for joining us today. We greatly appreciate your attention and interest in Black Hills Corporation. Once again, I thank our team for the great quarter, and we're hard at work in this quarter to deliver results on behalf of our shareholders and deliver great service to our customers. So thank you for joining us.

Operator^ Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Good day.