

**ALLETE**

**Moderator: Al Hodnik  
April 29, 2011  
10:00 a.m. ET**

Operator: Good day, and welcome to the ALLETE First-Quarter 2011 Financial Results call. Today's call is being recorded. Certain statements contained in the conference call that are not descriptions of historical facts are forward-looking statements, such as terms defined in the Private Securities Litigation Reform Act of 1995. Because such statements include risks and uncertainties, actual results may differ materially from those expressed or implied by such forward-looking statements.

Factors that could cause results that differ materially from those expressed or implied by such forward-looking statements include, but are not limited to, those discussed in the filings made by the Company with the Securities and Exchange Commission. Many of the factors that will determine the Company's future results are beyond the ability of management to control or predict.

Listeners should not place undue reliance on forward-looking statements, which reflects management's views as the date hereof. The Company undertakes no obligation to revise or update any forward-looking statements or to make any other forward-looking statements, whether as a result of new information, future events, or otherwise. I would now like to turn the conference over to your host for today, Mr. Al Hodnik, President and CEO. Sir, you may begin.

Al Hodnik: Good morning, and thank you for joining us. Mark Schober, ALLETE's Chief Financial Officer, is also with me today. As you know, we reported our first-

quarter earnings results this morning. I'm pleased with the start to the year, both financially and operationally, at Minnesota Power, Superior Water, Light and Power, and BNI Coal. Before Mark discusses the financial results, I would like to update you on some of our highlights for the quarter.

In early March Minnesota Power received large power nominations for the upcoming May to August time frame. Total nominations received indicate our industrial customers plan to produce at or near full capacity levels through August. These large industrial customers have a significant impact on the economy of northern Minnesota. So this is certainly good news for our entire region. We will receive nominations for the final 4 months of 2011 in early August. Incidentally, demand nominations indicate production levels are on track to exceed 2010 performance.

With regard to new industrial development in our region, Essar Steel Minnesota continues to move forward with construction of its planned taconite mining and pellet-plant operation within the city of Nashwauk. Hundreds of construction workers are already on site working on this massive undertaking.

Earlier this quarter, we announced a long-term electric-service agreement with the city of Nashwauk to provide all of their electric power supply on a wholesale basis. This in part to serve local community needs as well as for Nashwauk to serve their larger retail customers, most notably Essar Steel. Essar steel has indicated that they plan to start up production at this facility in 2012. We will keep you posted on their progress, as well as the progress of other potential new customers within the Minnesota Power service territory, all of which represent a significant growth opportunity for ALLETE as we go forward.

Shifting to our renewable energy growth initiatives, this quarter, we submitted our plans to the Minnesota Public Utilities Commission regarding the Bison 2 wind project in North Dakota. This \$160 million project will develop 105 megawatts of wind energy, scheduled to be in service by the end of 2012. Upon approval, this project will be eligible for current cost recovery and will be an economical source of renewable energy for our customers.

Our transmission investment and reliability objectives are also advancing, as construction began in January on the Bemidji-to-Grand Rapids 230-kilovolt line project, a project we are participating in through the CapX 2020 initiative. We are participating in 2 other 2020 projects currently, and plan to invest between \$100 million and \$125 million in them by 2015.

As you can see, in addition to having a solid financial quarter, we continue to move forward with all growth elements within our broader strategy. Now I will ask Mark to provide the financial details, and then I will make some additional comments before we take your questions. Mark?

Mark Schober: Thank you, Al, and good morning everyone. I would like to remind you that we filed our 10-Q this morning, and I encourage you to refer to it for more details. For the first quarter, ALLETE reported earnings per share of \$1.07 on net income of \$37.2 million. The 2011 quarterly results included the reversal of a \$6.2 million, or 18 cents per share, deferred tax liability related to a revenue receivable that Minnesota Power agreed to forgo as part of a 2010 rate-case stipulation and settlement agreement. Under this agreement, the Company will capitalize, as part of rate base, \$20.5 million to property, plant, and equipment.

Last year's first quarter reported earnings per share was 68 cents on net income of \$23 million. Net income in 2010 was reduced by a \$4 million after-tax, or 12 cents per share, charge due to the elimination of the deduction for expenses reimbursed under Medicare Part D. Excluding these 2 nonrecurring items, earnings per share was 89 cents on an income of \$31 million this quarter, compared to 80 cents on net income of \$27 million in 2010.

I will now provide details on a regulated operations segments, which includes Minnesota Power, Superior Water, Light and Power, and our investment in American Transmission Company. Net income for this segment was \$38.4 million for the quarter, compared to \$24.9 million for the same period in 2010. Excluding the 2 items I just mentioned, the increase over 2010 is attributable to a 29 percent increase in industrial customer power use and higher rider

revenue, partially offset by 33 percent decrease in sales to other power suppliers and higher expenses. Total kilowatt hour sales were up 5 percent from the same period a year ago. Total regulated operations revenue increased \$6.9 million, or 3 percent over 2010.

In addition to the combined impact of increased industrial power use and decreased sales to other power suppliers, \$2.8 million of this increase was from higher renewable rider revenue due to a higher capital expenditures related to our Bison 1 and CapX 2020 projects. Regulated operations – operating and maintenance expense increased \$1.4 million, or 2 percent, over the same period in 2010. The increase reflects higher labor and benefit costs and outage expenses at our generating plants. Depreciation expense increased \$2.2 million, and interest expense was up \$1 million for the quarter, both directly attributable to the capital-investment program at our regulated operations.

Earnings from our investment in the American Transmission Company for the quarter were in line with 2010 results. Income tax expense decreased \$12 million, or 54 percent, from 2010, primarily due to the reversal of a \$6.2 million deferred tax liability related to a revenue receivable of Minnesota Power agreed to forgo as part of a stipulation settlement agreement in its 2010 rate case.

Also, contributing to the decrease was a nonrecurring income tax charge of approximately \$4 million, resulting from the elimination of the deduction for expenses reimbursed under Medicare Part D due to the Patient Protection and Affordable Care Act in the first quarter of 2010.

Our effective tax rate for the first quarter of 2011 was 18.1 percent. Including the reversal of the \$6.2 million deferred tax liability, the effective tax rate was 31.8 percent. We anticipate the effective tax rate for the year will be approximately 30 percent. The investments in other segments reported a net loss of \$1.2 million, compared to a net loss of \$1.9 million in 2010.

Contributing to the decreased losses were lower losses at ALLETE properties due to reduced operating expenses. Contributions from BNI Coal were in line with 2010 results for the quarter.

Finally, our largest share balance over last year had a dilutive impact of 3 cents per share for the quarter. Our cash flow was strong for the quarter. As of March 31, we had a 22 percent increase in cash from operating activities and a 44 percent debt-to-capital ratio. In summary, we are pleased with our financial results in the first quarter and are excited about our prospects for the full year. Al?

Al Hodnik:

Thanks, Mark. I am very pleased with our first-quarter progress, and I am anticipating continued strong performance for 2011. Though we continue to make progress, including our improved first-quarter earnings, we still do not anticipate earning our allowed regulated return on equity this year. However, based primarily on the improvements in sales to our industrial customers, we now project our 2011 earnings to fall within a range of \$2.40 to \$2.60 per share.

Before we take your questions, I would like to make a few additional comments. I mentioned earlier that we submitted our plans for the Bison 2 wind project to the Minnesota Public Utilities Commission. We expect to begin construction on the Bison 2 project during the fourth quarter of this year. As you may know, last year we completed construction of the first phase of our Bison 1 project, and those turbines are now in service. Site preparation for the second half of our Bison 1 project is underway here this spring, and we expect it to be completed and in service by December of this year.

Upon completion of both Bison 1 and Bison 2, our North Dakota wind initiative will have grown to nearly 190 megawatts, with prospects for more to come. Our Bison wind projects, as well as the CapX 2020 projects mentioned earlier, are all included in our current 5-year capital-expenditure plan. As a reminder, we project this plan will result in rate-base growth of approximately 20 percent through 2015.

Turning to customer growth opportunities, there are a number of industrial projects in various forms of development within and around Minnesota Power's service territory besides the Essar Steel taconite facility mentioned

earlier. If they all come to fruition, combined, they represent a potential increase in load of about 33 percent for Minnesota Power over the next 5 years. In addition to potential customer growth and our capital expenditure plans, we are also committed to taking the actions necessary to earn our allowed rate of return at our regulated businesses. While we pursue other energy-centric growth opportunities, either within our regulated businesses or outside of them, these are truly exciting times for ALLETE. At this point, I'll ask the operator to open up lines for your questions.

Operator: Thank you. If you have a question at this time, please press star then one on your touchtone telephone. If your question has been answered or you wish to remove yourself from the queue, please press the pound key.

And our first question comes from Larry Solow with CJS Securities.

Fred Bonacore: Yes, good morning. This is actually Fred Bonacore calling in for Larry.

Male: Hi, Fred.

Fred Bonacore: Good morning. First question just relates to your guidance. It seems like even with the increase, just given the strength that you're seeing through the industrial end market, that you're tracking towards the high end of that guidance. Is there any way you can give us a sense for what are the factors that would put you in the high end versus the low end of the guidance? What are the variables involved in that guidance we should be looking for to get a sense of where you will fall, or where you may fall in? Thank you.

Mark Schober: Yes, sure, Fred. Again, when look at our guidance, the \$2.40 to \$2.60, the issues that we see coming out that create that uncertainty – the first one would be our taconite combination for the last 4 months of the year as Al referred to. We don't have those nominations in-house, and we don't know where those folks will be operating. So that will impact it.

Real estate results at ALLETE Properties could be some sales. We're planning on some sales there. If they don't close, that could cause some deviations. And then just normal operations. Weather impacts us a little bit.

Storms, et cetera, could cause some variance from that guidance. And then I'd also like to highlight, too, that if you recall the first quarter is typically ALLETE's strongest quarter. So this is very – earnings pattern is very similar to what we had last year, so we don't anticipate having earnings at the level we did for the first quarter for the remainder of the year.

Fred Bonacore: OK. That's very helpful. Thank you. And then secondly, can you comment on the recent JV with ATC and Duke Energy? Any impact expected from that on ALLETE?

Al Hodnik: No, we're not expecting any direct impact. I mean it's a joint venture that allows ATC and Duke to explore transition projects together as partners, but it also still allows both to pursue transmission projects individually. So you know all things being equal, I think it enhances ATC's opportunities to explore other transmission projects and it may indirectly increase the growth rate or the size and expansion rate of ATC, but it's not going to directly impact ALLETE at this point in time.

Fred Bonacore: OK. Thank you very much.

Operator: And our next question comes from the line of James Bellessa with D.A. Davidson & Company.

James Bellessa: Good morning.

Male: Good morning, Jim.

James Bellessa: Just to make sure it's clear, the new guidance range excludes this 18 cent benefit that you received in the first quarter?

Mark Schober: No, Jim, it includes that 18 cents, and our original guidance included that 18 cents, too. So it's in both numbers.

James Bellessa: Yet, you excluded last year guidance for the healthcare reform legislation. Why won't you be following the same pattern and excluding in guidance these one-time items?

Mark Schober: Yes, the difference, Jim, is because that Medicare D came in after we issued our guidance, so that was why it's excluded. We anticipated, as we finalize the 2010 rate case, that the stipulation agreement would be in there. So that's why it's included in the guidance. It's simply the fact of circumstances that we know at the time we issue our guidance.

James Bellessa: In your utility business, the depreciation kicked up. You were running \$18 million, \$19 million to \$20 million, and then it jumps up in the first quarter to \$21 million. Can you explain that, and is this a maintainable level?

Mark Schober: Yes, the depreciation expense continues to grow with our capital expense program. So we're – last year, we put in about \$250 million property, plant, and equipment, you'll see – or CapX. You'll see this year similar numbers, so you'll continue to see growth in depreciation. So nothing unusual there, Jim. Just tracking growth in our invested plan.

James Bellessa: And you've filed for appeal of your interim rate decision based on that exigent-circumstance ruling a year ago. What are your chances of prevailing?

Mark Schober: Jim, I am unable to predict what our chances are of prevailing. Our focus there is the application of those exigent circumstances and to clarify those issues for future rate cases as we move forward. So it goes to the court and then hopefully back to – remand it back to the MPUC for a decision. So there are several steps there, and we're certainly unable to predict where that will end up.

James Bellessa: So you're trying to remove from the commission's tool basket the ability for them to call on exigent circumstances willy-nilly?

Mark Schober: It's really the application of exigent circumstances in future rate cases, yes. It's to clarify how that works.

James Bellessa: Thank you very much.

Al Hodnik: Thank you, Jim.

Operator: Again, if you have a question, please press star, followed by the one key.

I'm sorry. I'm showing no further questions in the queue.

Al Hodnik: All right. Well, thank you everyone. We look forward to visiting with you again after the close of our second quarter.

Operator: Ladies and gentlemen, thank you for your participation in today's conference. This concludes the program. You may all disconnect. Everyone have a great day.

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