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DTE - Q3 2013 DTE Energy Company Earnings Conference Call

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OVERVIEW:

DTE reported 3Q13 operating EPS of $1.13.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the DTE Energy-hosted third-quarter 2013 earnings release conference call. Today's conference is being recorded. (Operator Instructions). At this time, I would like to turn the conference over to Mr. Dave Meador. Please go ahead, sir.

Dave Meador - *DTE Energy Company - EVP, CFO*

Thanks, Andrea, and I apologize to you for that music while you were on hold there. We were hoping to have the Tigers theme song playing while you are on hold, but that didn't work out so well this year. Maybe next year.

But good morning and welcome to our third-quarter earnings call.

Before we get started, I encourage you to read the Safe Harbor statement on page 2, including the reference to forward-looking statements.

So moving on to slide 3, with me this morning are Peter Oleksiak, our Senior VP of Finance; Dan Brudzynski, our Vice President and Treasurer; and Anastasia Minor, our Director of Investor Relations. I also have members of the management team with me if needed during the Q&A session.

Looking at slide 4 on the agenda here, we are going to provide results on the third-quarter performance and also update you on our financial goals for the rest of the year.

Gerry Anderson will be presenting at the EEI conference in a couple of weeks, where he will provide you an in-depth business update and details on the growth plans.

So this morning, I will focus the call on the quarter and the remainder of the year, but as always, I would be happy to take questions on any topic.

So moving to slide 5, this is an overview of our business strategy and investment thesis. Our growth plans for the next 10 years at both utilities are robust. Our electric utilities' growth over the next five years is driven by operational investments, environmental controls, renewable energy, and then if you look out to the second five years, new generation, which is going to replace some of our coal fleet.

At the gas utility, growth was driven by infrastructure investments and meter relocation. We also have meaningful low growth -- low-risk growth at our non-utility businesses, and they provide diversity both in earnings and geography. And as I said, we will provide more details for all these businesses at EEI in a couple weeks.

We operate in a very supportive regulatory environment and we work hard every day to continue to earn that construct. Our effort, as you know, begins with highly-engaged workforce and an ongoing focus on continuous improvement. This enables us to continue our cost-savings track record, and also, it enables our utilities to consistently earn their authorized returns.

We also continue to focus on operational excellence and customer satisfaction that we believe is distinctive in our industry.

Our dividend payout range is 60% to 70% of earnings, and we target a strong BBB credit rating. Our strategy, altogether, provides for a consistent 5% to 6% earnings growth, an attractive and increasing dividend, and all of that with a strong balance sheet.

If you turn to slide 6, this is our earnings and dividend growth slide that we have shared with you in the past. We remain confident that our growth plans will deliver our 5% to 6% earnings-per-share growth. In fact, for this year, we are tightening our range on our guidance of $3.95 to $3.14, and we're going to affirm our $4.05 midpoint, which Peter will go over in a little bit more detail in a minute.

The midpoint provides 6.6% growth over our weather-normalized earnings of last year, which were $3.80. We're also reiterating our confidence in our 2014 early-outlook midpoint of $4.27 per share, which provides about 5.5% growth and which is right in line with our long-term growth outlook.

But back to the chart, if you look on the left-hand slide, you can see we have actually exceeded our commitment of 5% to 6% growth by delivering 7% annual growth from 2008 to 2014. As you know, we increased our dividend each year starting in 2010, and earlier this year, we increased it to $2.62, which was a 5.6% increase. Based on the $4.05 earnings-per-share midpoint this year, that dividend gives us about a 65% payout. And as our earnings continue to grow, we would expect to grow our dividend over time.

And then on the bottom, you can see our overarching goal is to earn $1 billion by 2017, and we are well on our journey to do that.

Turning to slide 7, the Michigan economic turnaround continues. We have actually one of the better economic growth rates in the nation, which, by the way, when Peter talks about our load numbers, it's directly reflected in our load growth. If you look at the measures that we track -- auto production, housing starts, new customers, unemployment, just to name a few metrics -- they all continue to trend very positively.

We're also being recognized by many external organizations in areas that demonstrate progress that Michigan is making. On the bottom of page 7, we have just highlighted a handful of these. If I included all of them, I would have to have more pages in the presentation.

As the state continues its strong economic comeback, the city of Detroit continues to work through the resizing of city government. Regarding the bankruptcy filing that happened earlier this year, this is the first step in Detroit's recovery and we believe the process will address its financial problems in a sustainable way.

We also continue to believe there will be no impact on DTE Energy as a result of the bankruptcy.

I realize how Detroit's often portrayed in the national news, which is not often showing the signs of the city moving forward and the progress that is really being made that we see every single day here. There's a lot of positive momentum on economic development and job creation in real estate development in the city.

For example, Google recently named Detroit one of seven new entrepreneur and technology hubs in the entire country. Detroit was one of the seven. So I'm very confident that Detroit and Michigan will continue this positive momentum and will come out stronger, both as a region and a state.

While I'm discussing the city and the state, it's a good time just to mention the energy policy work that is going on in Michigan. The MPSC is currently issuing its fact-finding reports. They came out as a collaborative work with stakeholders over the last year. Final reports on the four areas, which were energy efficiency, renewable energy, choice, and then other considerations, and an example on that bucket would be electric reliability, are expected to be issued by the end of November.

These findings should help set the foundation for the Governor's long-term energy policy recommendations. We expect the Governor to take a balanced approach for the state, ensuring that the policy makes sense for Michigan residents.

Now moving to our financial overview on slide 8, we continue to have strong results in 2013 and we are very confident in our earnings guidance midpoint, and we have tightened the guidance range, as I've mentioned, to $0.20. Our year-to-date operating earnings of $3.09 per share are up $0.01 from 2012. Third-quarter operating earnings were $1.13 per share, compared to $1.30 last year.

It's important to remember that we experienced extremely warm weather last year. In fact, it was one of the warmest summers on record and it provided the electric utility $40 million of favorability in the third quarter of last year. This year's electric sales returned to a more weather normal condition, and like the second quarter of this year, we experienced lower benefit expenses due to our benefit design changes that we made.

Our gas utility earnings returned to a more typical performance in the third quarter. Last year, the gas business benefited by a number of one-time items that are not repeated this year. We are very confident in our earnings targets for gas and we are raising our guidance for the segment to a range of $125 million to $130 million, which is a $10 million increase, and Peter will take you through the details in a minute.

The balance sheet remains strong, and we generated approximately $1.7 billion in cash from operations year to date. We are increasing our cash-flow guidance for 2013, primarily due to improved working capital and summary timing of capital investments at DTE Electric. So we're on track to meet our balance-sheet goals for 2013 with a strong credit rating from each of the agencies.

Before I turn it over to Peter, I just wanted to comment briefly on the challenges around quarterly earnings guidance, which we don't provide, and the consensus that comes out from sell-side analysts. As you know, our overarching goal is to deliver for the year both our guidance at midpoint and to earn our authorized return at both utilities, and we have an established track record of doing that.

We have explained in the past how we are managing our O&M, primarily around weather, with our lean and invest strategy. This year, changes in retiree health care triggered $60 million to $70 million of favorability earlier in the year, and when you couple that with the first-quarter gas favorability, we started out the year in a very strong position. So we initiated higher O&M or reinvestment in the second quarter and the third quarter.

Normally, reinvestment based on weather favorability would have been timed later in the year, so we actually launched our reinvestment strategy much earlier than we do normally. But given that background, even with lower trading earnings, we are very confident in the $4.05 for the year. And as you know, we always plan the year and the forward years with some contingency in our planning.

So with that background, let me turn it over to Peter and he'll go through some more details on the quarter.

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Thanks, Dave, and good morning to everyone.

I would like to start with slide 10 and the third-quarter earnings results. For the quarter, DTE Energy's operating earnings are $1.13. As a reminder, there is a reconciliation to GAAP reported earnings included in the appendix.

Of the two utilities, DTE Electric contributed $1.02 and DTE Gas, which typically incurs an operating loss in the third quarter, came in at a $0.07 loss. The non-utility segments combined to earn $0.21 for the quarter. The drivers for the non-utility results are gas storage and pipelines at $0.09; power and industrial projects at $0.15; and the energy trading segment had a loss of $0.03. Finally, corporate and other had a loss of $0.03, as well.

Let's move to slide 11 and a summary of the quarter-over-quarter performance by segment. DTE Electric contributed $15 million less to earnings year over year and DTE Gas had a decrease in earnings of $17 million. I will cover details on both our electric and gas utilities in a moment.

Operating earnings for our two non-utility growth segments are up a combined $7 million in the quarter, offset by a loss in our trading business. In our gas storage and pipelines segment, for the quarter, earnings growth in our pipeline assets is partially offset by lower storage earnings. Incremental pipeline growth is starting to flow through to the bottom line in the second half of the year as volumes increase on our Bluestone and related gathering investments.

Power and industrial earnings are also higher for the quarter, driven by increased earnings from our reduced emission fuel projects and our on-site energy project portfolio acquisition that occurred last year.

Year-over-year growth in this segment will continue for the remainder of the year.

At energy trading, accounting for economic hedges related to longer-term transactions and economic earnings not yet realized for accounting purposes is driving the loss for the quarter. The economic income for the quarter is comparable to last year. In the appendix, we have included our standard energy trading slides, which show both economic and accounting performance.

Finally, our corporate and other segment came in favorable by $4 million from last year, due primarily to lower interest and taxes.

I would like to now turn and talk to the two utilities in more detail, starting with the electric utility, if you turn to page 12. The DTE Electric earnings variance was mainly driven by the return to relatively normal weather this quarter, compared to the 2012 abnormally hot weather. Actually, cooling degree days last summer in the quarter were 40% higher than normal, compared to this year, which actually was relatively close to weather normal. Now this weather difference is driving $40 million in lower earnings in 2013.

I know individuals on this call are always interested in what is happening with our underlying electric service territory load. We continue to see growth in underlying load with temperature-normalized sales growth at 3% in the quarter, compared to the same quarter last of year. And actually for the year, on a year-to-date basis, normalized sales were 2% higher in 2013 and actually is driven by growth in all of our segments.

Also driving year-over-year earnings is reduced benefit expense. Dave mentioned that in his opening remarks. As you recall, on the first two quarterly calls, I talked about structural cost changes we made to our retiree health care plans. This benefited electric earnings this quarter by $14 million.

Now typically I don't talk about the next quarter in the call, but looking to the fourth-quarter drivers for the electric business, we will see a lot of quarter-over-quarter growth driven by this benefit expense reduction, which will flow and improve the fourth-quarter results, and also by significant reinvestment spending last year that occurred in the fourth quarter that's not occurring this year.

Just as a reminder, last year we did spend $20 million in reinvestment, really driven by that weather favorability, with the majority of that occurring in the fourth quarter.

Moving on to DTE Gas, on slide 13, as I mentioned earlier, the gas business typically sustains a small loss in the quarter. The fact that DTE Gas showed earnings of $4 million in the third quarter in 2012 is atypical for the gas company and is driven mainly by short-term cost-reduction actions, or lean actions, the Company took to offset a slow start to the year last year.

During the earnings call last quarter, I talked about reinvestment into our core utility assets that would be occurring this year. For DTE Gas, this drove $6 million of the variance of this quarter from 2012.

An increase in rate base-related expenses is the primary driver in the other variance of $5 million.

Let me now move to the total enterprise and the guidance for the remainder of the year. As shown in slide 14, we're narrowing our EPS guidance from $0.30 to $0.20, while we are maintaining our midpoint of $4.05 for all of our segments. In addition, we are remixing our 2013 earnings guidance, reflecting strong earnings at our gas utility and economic earnings that will not be realized for accounting purposes this year at our energy trading segment.

At DTE Electric, growth in electric sales, as well as renewable investments and lower benefit expense, have funded our reinvestment activities. We expect DTE Electric to achieve the guidance range of $480 million to $490 million.

At DTE Gas, year-to-date earnings have been very strong, driven by favorable weather, higher weather-normalized consumption, and lower benefit expense. We will continue O&M reinvestment in the last quarter of the year at our gas utility segment, funded primarily by this usage and benefit expense favorability.

As I mentioned earlier, gas storage and pipeline and power industrials project segments are on track to achieve their guidance with the Bluestone Pipeline and gathering system ramp-up and the incremental earnings associated with a reduced emission fuel business line flowing through the remainder of the year.

That concludes an update on our earnings for the quarter. Now I would like to turn the discussion over to Dan Brudzynski, who will cover cash flow and capital expenditures.

Dan Brudzynski - *DTE Energy Company - VP Treasurer & IR*

Thanks, Peter, and good morning, everyone.

Beginning on slide 16 in our year-to-date cash flows, through September, cash from operations is $1.7 billion, which is comparable to 2012 levels. Capital spending was slightly higher than last year, due to increased spending at the electric utility and increased investments in our Bluestone Pipeline and its related gathering assets.

Electric utility capital is higher due to increased spending on our nuclear operations, system reliability, and environmental projects, partially offset by the re-timing of renewable energy spend.

Overall, DTE's net cash is down slightly year over year.

Slide 17 lays out this detail for the year-to-date capital expenditures. You can see the increases in electric utility capital, as well as the non-utility businesses, which, as I said earlier, reflects increased investments in Bluestone. The gas utility is comparable to 2012's levels.

Turning to slide 18 and the look ahead for 2013, as David mentioned earlier, we are increasing our cash flow guidance for 2013, with cash from operations expected to be slightly higher than the original guidance and capital spending expected to be slightly lower. Our increased cash guidance is driven by the timing of surcharge collections at DTE Electric -- our prior guidance had assumed recovery of these undercollections over 2013 and 2014 -- and also lower corporate tax payments.

The change in capital is primarily due to the re-timing of dry sorbent injection, or DSI, installations, based on a one-year compliance extension that was granted by the Michigan Department of Environmental Quality. And you can see that detail in the table on the right of that page.

Then finally, finishing up on slide 19, as David mentioned, our balance sheet remains strong with leverage and FFO metrics in line with our targets. Our financing plan is on track as we have issued approximately $300 million of equity into our benefit and DRIP plans. By year-end and the remaining DRIP plan in effect, we expect total equity issuance for the year to be slightly over that $300 million level.

We have issued about $800 million in debt and continue to have sufficient liquidity. And with that, I will turn the discussion back over to Dave for some concluding comments.

Dave Meador - *DTE Energy Company - EVP, CFO*

Thanks, Dan. Let me wrap up on slide 21. As we laid out for you, we're on track to reach our 2013 earnings-per-share guidance, and that we narrowed our guidance from $0.30 range to a $0.20 range with a $5.05 -- $4.05 midpoint. We are increasing our cash-flow guidance, and Dan took you through that. The balance sheet is exactly where we want it to be.

Going forward, our robust operational and utility investments, together with low-risk non-utility growth opportunities, are expected to provide 5% to 6% annual earnings-per-share growth and dividend growth.

As I mentioned, we will be at EEI in a little over two weeks and we hope to see many of you there. Gerry Anderson will be providing a detailed business update for each of our business segments. The presentation that Gerry will provide will begin at 11.15 Eastern Standard Time on Tuesday, November 12. For those of you not going to EEI, you will be able to join that webcast through our investor relations website.

And Andrea, with that, we would like to open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Kevin Cole, Credit Suisse.

Matt Davis - *Credit Suisse - Analyst*

It's actually Matt Davis. Just a quick question on the O&M reinvestment program and the timing for this year in the fourth quarter, and looking at it versus last year. I know you guys said that you had spent $20 million extra last year, and then this year, you had reaccelerated that earlier in 2Q and 3Q. And so, what kind of year-on-year changes are we looking at in the fourth quarter?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Last year was predominantly in that fourth quarter, so I'd say about three-fourths of that, and then this year, we have had some small remaining amount, but actually the majority of it, if not all of it, has been spent already this year. Really, you'll see that fourth quarter last year flow to the bottom line.

Matt Davis - *Credit Suisse - Analyst*

And how will this level of O&M flow into 2014? Should we expect this is a normalized level of O&M or an increase, decrease?

Dan Brudzynski - *DTE Energy Company - VP Treasurer & IR*

The reinvestment really is on a year-by-year basis, so if you look at normalized O&M, I would take the reinvestment off of that, and we have described before, basically, going into the year, we have a couple of different plans. One of them is the weather normal plan. Other one is more of an invest plan, if we get additional revenue in.

So next year, we are projecting out, as we talked about, productivity and a relatively flat O&M, but as we get into the year, we will make the decision whether we reinvest.

Dave Meador - *DTE Energy Company - EVP, CFO*

So long term -- first of all, we're still back at our 2005 O&M levels, which is about $1.5 billion, and our goal is to hold it at $1.5 billion through the next several years.

So year to year, you might get some shifting back and forth, certainly quarter to quarter. But quarter over quarter, as you see this year, you will see that happen, and we want to try to help you through that. So if you are looking forward, I would just assume that we are going to hold O&M flat, as we have been, which is offsetting inflation and also offsetting new O&M that's coming into the business.

Matt Davis - *Credit Suisse - Analyst*

Okay, and then, secondly, what kind of guidance are we -- should we expect to get at EEI? Are we going to be getting additional CapEx guidance, additional segment earnings guidance? What level of detail should we be expecting?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

We definitely will talk a little more detail around 2014. So you can expect an update around 2014 guidance.

Dave Meador - *DTE Energy Company - EVP, CFO*

And then, we have already laid out, as you know, 10 years of CapEx for the utilities. There probably will be some refinement about -- there will probably be some more clarity about our thinking about the transformation of our coal fleet over time, and how that plays out and plays, hopefully, into the Governor's new energy policy and, hopefully, what we see transpiring in Washington.

So I think we have a pretty good story to tell about, over time, how some of the coal fleet will close just naturally because it's coming down to life and how that will be replaced, and do that in conjunction with expanded renewable energy policy and so on. So I would expect Gerry to go into more detail on the utilities and energy policy, and then clearly more details on the non-utilities.

Matt Davis - *Credit Suisse - Analyst*

Okay, thank you very much. See you guys in a couple weeks.

Operator

Andrew Weisel, Macquarie.

Andrew Weisel - *Macquarie Capital Securities - Analyst*

It sounds like the utilities are strong. I appreciate the color you just gave on the O&M reinvestments and 3% weather-adjusted load growth at the electric business, if I heard you right. Any change to your plans about the timing of the next round of rate case filings?

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Dave Meador - *DTE Energy Company - EVP, CFO*

No change right now (multiple speakers). We're still thinking that we're going to be filing next year for the electric business, with new rates in 2015. And the gas business, we have the infrastructure tracker, and that, with ongoing cost control, is going to allow us to stay out three years or longer. So, we go into 2014 with a lot of stability and no rate cases.

Andrew Weisel - *Macquarie Capital Securities - Analyst*

Great. Next question, on the pipelines. It sounds like Bluestone is ramping up pretty nicely. Can you give us an update on Nexus, the Utica pipeline? Specifically, I'm curious what you are hearing from producers right now, when you think contracts might start being signed, and what might be a range of possible in-service dates.

Dave Meador - *DTE Energy Company - EVP, CFO*

This is one of the projects that Gerry will talk more about at EEI, but just to generally give it some tone, we still get positive indication, so not only the demand for the gas in Michigan and Ontario at the Dawn connection, but also, as all of us are watching the wells in the Utica play, a lot of positive signs there.

So I think what we are thinking our way through right now is as the Utica develops, which pipes in the region go through the expansion first. So either they are going to be additional compression or looped, and then at what point in time are there going to be new pipes built.

And as this plays out, I still would characterize this as very positive, and the timing right now in terms of in-service, our thinking has not changed. I think it's in the 2016-2017 timeframe, but again, we will give you more details at EEI.

Andrew Weisel - *Macquarie Capital Securities - Analyst*

Great, and then, lastly, just for the trading business, it sounds like some timing issues at accounting earnings versus economic. Given that you are basically a small loss year to date versus your updated guidance range, should we assume that catches up in the fourth quarter, or might some of this fall into 2014? And for now, are you still comfortable with the $10 million to $30 million guidance range for 2014 earnings?

Dave Meador - *DTE Energy Company - EVP, CFO*

You want to answer that, Peter?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Yes, I will answer that. Yes, I guess, first, I can talk about the guidance -- the overall timing. We do have in the appendix, we do lay out the difference between the economic and the accounting, and there is a $14 million timing in the quarter.

A few million of that will come back in the fourth quarter. The rest of that, actually, will play through on 2014 and 2016, and actually, I can take a moment. I need to talk a little bit more around the timing that we are seeing. Actually, there is two pieces on this.

One of them is related to economic hedges, and we have talked about this in the past, this one-sided accounting that occurs. So as we hedge in transactions, the accounting related to those hedges actually get mark to market versus more accrual-based of [if one would be] a transaction.

Actually, there is a bigger piece of this timing that is tied to the mix of the types of transactions. Actually, this business, we are moving more towards -- from pure trading type of transactions that get immediate accounting and economic recognition to transactions related to origination deals and contracts tied to assets, and actually, the accounting of this flows with the transaction. That describes some of the longer tail on this roll-on is really tied to those transactions.

Andrew Weisel - *Macquarie Capital Securities - Analyst*

Okay (multiple speakers) thank you.

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Andrew, one other, I guess you were talking about the guidance. Actually, the guidance, revised guidance, is $5 million to $15 million, so we did take down the guidance for the (multiple speakers)

Andrew Weisel - *Macquarie Capital Securities - Analyst*

That was for this year; I was asking about next year.

Dave Meador - *DTE Energy Company - EVP, CFO*

We are thinking our way through that (multiple speakers). My general sense is, as you know, this is not part of our growth story at all.

And over time, hopefully what you're going to see is our other -- you look at our non-utility businesses in the midstream and power and industrial, they are growing 15% to 20% per year, and just as a strategy working with you all, I want to de-emphasize trading. And so, we're working our way through that and either we will have an update at EEI or when we finalize our guidance in January.

Andrew Weisel - *Macquarie Capital Securities - Analyst*

Understood. Thanks a lot.

Operator

Matt Tucker, KeyBanc Capital Markets.

Matt Tucker - *KeyBanc Capital Markets - Analyst*

Most of my questions have actually been asked and answered. I guess I wanted to ask the first question in a different way. When you look at the implied fourth-quarter guidance on the electric side, it implies something like $30 million to $40 million year-over-year earnings growth, or 50% plus. Given weather was only drag about $5 million last year, and assuming normal weather this year, should we see most of that is coming from O&M, or could you just talk a little bit about the drivers there?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

It is probably split half -- some of that benefit favorability we are seeing in the third quarter, so you saw that level come through. That same level is going to come through in the fourth quarter.

And the other, as I mentioned, we had a $20 million reinvestment last year. About three-fourths of that is going to flow through favorability in the fourth quarter.

And actually, you look at the fourth quarter, the implied fourth quarter, it is actually pretty typical for a fourth-quarter result for an electric utility. So actually, it is getting it back to more of a typical fourth-quarter result.

Matt Tucker - *KeyBanc Capital Markets - Analyst*

Got it. Thanks. And kind of a similar question, maybe similar but opposite on the gas side. The guidance implies a pretty steep year-over-year drop-off. Is that, again, primarily just on O&M reinvestment?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Yes, that is correct.

Matt Tucker - *KeyBanc Capital Markets - Analyst*

Got it, thanks. That's all that I had. See you at EEI.

Operator

(Operator Instructions). Julien Dumoulin-Smith, UBS.

Julien Dumoulin-Smith - *UBS - Analyst*

So you guys already asked about -- or answered regarding Nexus, but on the Bluestone side, you had some developments in the quarter regarding new agreements, et cetera. Could you perhaps provide a little bit more color about added CapEx and perhaps further achievements after the Southwest deal?

Dave Meador - *DTE Energy Company - EVP, CFO*

I would just tell you this is an exciting time for us, an exciting time for that segment. So as you know, in the whole midstream space, the estimates over the next 10 years is there is going to be $1 trillion of investments made because you have to get this gas to market. And we're putting a lot of our muscle into not only what we can do on Bluestone and the Bluestone area with Southwestern and other producers, but we're also looking at what other opportunities there could be for us.

So I would just characterize this as very positive, and not that we are coming out with any major announcements at EEI, but it's just something I think Gerry Anderson will talk more about at EEI, and then as things develop here, certainly we will provide more color around that. But we are talking to Southwestern as we speak about deepening and furthering our relationship not only in that basin, but possibly in other basins.

Julien Dumoulin-Smith - *UBS - Analyst*

Great, and just -- I presume that would involve a CapEx update at EEI, just to be clear?

Dave Meador - *DTE Energy Company - EVP, CFO*

Yes.

Julien Dumoulin-Smith - *UBS - Analyst*

Great. And then, just going back to the trading side, just again to be clear on this one, clearly not necessarily a reversal in 2013, but as you think about the accounting risk as the operating -- or [rather], I suppose it's the description -- that would materialize in your operating earnings beyond 2013, so perhaps there is a little bit of a tailwind here into 2014 and subsequent years.

Peter Oleksiak - *DTE Energy Company - SVP Finance*

(Multiple speakers) that's part of the strategy. As you get these more origination or non-derivative type of transactions, it does build some income base for this business over multiple years.

Julien Dumoulin-Smith - *UBS - Analyst*

Got you. Is there anything in particular you can point to for subsequent years here?

Dave Meador - *DTE Energy Company - EVP, CFO*

Not at this time.

Julien Dumoulin-Smith - *UBS - Analyst*

Okay, great. Thanks again.

Operator

Greg Gordon, ISI Group.

Greg Gordon - *ISI Group - Analyst*

You mentioned pretty specifically in the context of answering another question that you expect to be able to hold your O&M absolutely flat over the next few years. Can you comment on what you are seeing, and I know interest rates have come back down from their peak, but in terms of what you're seeing in terms of change in discount rate on your pension plans, and how significant an O&M reduction on the GAAP pension expense you might be looking at, and what your funding status might look like, given where interest rates are today?

Dave Meador - *DTE Energy Company - EVP, CFO*

Sure. Actually, before I do that, I want to correct myself. On O&M, we are striving for flat O&M, and at the same time, we are exploring further structural cost changes over time, and it's part of our strategy around trying to keep rates as low as possible for customers.

So we have this one goal for O&M, and at the same time, we are looking for opportunities for step-function changes, and I think at EEI we will talk more about that.

An example of that is what we just did with retiree healthcare, where this year we are going to -- you're going to see $60 million to $70 million of benefit, and on an annualized basis, next year it is $70 million to $80 million on retiree healthcare, so we continue to look for opportunities on that.

On the pension side, and I will ask Peter or Dan for help, the discount rate continues to move. You only measure that once a year, so you measure that at the end of the year. But we expect, with interest rate movement here, the discount rate will go up, and that, in addition to real good returns on our assets, we are seeing our funded status go back up. Do you have those numbers, Peter?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Yes, and the funded is over the 80%, so we are well on our way over the next few years to get fully funded.

And I guess on the benefit, and as we talked about this and the strategy with the retiree healthcare, it really is part of our bridging strategy, coupled with the need to stay out, as well as our affordability for our customers. And actually, next year, there is another portion since we had two changes -- we had one in our salary plan and our union plan, and actually our union plan, the benefits are flowing in the second quarter on. So we will see some additional favorability, and that's why the move goes up to $70 million to $80 million from the $60 million to $70 million.

So, and as you mentioned, there is another tranche of favorability that is coming related to discount rates, and actually, we like that. For next year, like I said, once we really settle in what that accounting is and what it's going to be, we will update you in terms of where we are at on our overall earnings, as well as investment plans within the utilities. And if this holds, it will be good for our customers as well, in terms of overall (multiple speakers)

Greg Gordon - *ISI Group - Analyst*

Just to be clear, this is completely away from retiree healthcare, but just on pension, given the way your performance has been and given where discount rates are trending, you would expect to have to fund less on a cash basis, A. And secondly, you would expect a significant reduction in your GAAP operating expense. Is that correct?

Dave Meador - *DTE Energy Company - EVP, CFO*

Right, over the next several years. So we -- as we mentioned, we are 82% funded, and we will have a couple of years of cash contributions. Our goal is to be fully funded by 2016.

We're already starting to shift our asset allocation in terms of immunizing our risk to future interest rate changes, so as we increase our funding, our cash contributions will be much less and our pension expense will be much less. And we will then have, hopefully, immunized ourselves to any future interest rate changes down the road.

Greg Gordon - *ISI Group - Analyst*

That's great. Thanks, guys.

Dave Meador - *DTE Energy Company - EVP, CFO*

You are spot on on that.

Operator

Jonathan Arnold, Deutsche Bank.

Jonathan Arnold - *Deutsche Bank - Analyst*

Just a quick one. I want to make sure I heard you right. You talked about 3% was the underlying electric sales growth. Was that the third quarter versus third quarter last year?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Yes, that was kind of a third quarter over third quarter.

Jonathan Arnold - *Deutsche Bank - Analyst*

And it seems to have picked up slightly as you've moved through the year. What is your best guess where you're going to finish the year, and how are you thinking about 2014 and beyond?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Yes, we think we are now -- on a total-year basis, we are going to be at the 2%. Actually, as you know, year to date we are at 2%. Residential, right now year to date is 2%. We think that will settle in at 1%, and then our industrial will be settling in about a 4% for the year.

So we're thinking 2%. There may be a little bias upwards on the 2%, but still thinking that it's going to be a 2% growth. And on a go-forward basis, we are looking at about a 1% growth, and that's actually including energy and efficiency, so net of efficiency.

Jonathan Arnold - *Deutsche Bank - Analyst*

1% net of efficiency going forward.

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Going forward.

Jonathan Arnold - *Deutsche Bank - Analyst*

Is that how to break down between the segments, roughly?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

I'd say it is probably residential relatively flat. That's typically how we have given usage and that's where your energy efficiency programs are, and both the commercial and industrial are pretty relatively equal and make up that 1%.

Jonathan Arnold - *Deutsche Bank - Analyst*

Okay, great. Thank you, guys.

Operator

Julien Dumoulin-Smith, UBS.

Julien Dumoulin-Smith - *UBS - Analyst*

Wanted to follow up here just on transmission, actually. Some of your peers out there have been talking about it, of late. Any thoughts to perhaps pursuing something comparable?

Dave Meador - *DTE Energy Company - EVP, CFO*

Not at this time. For those of you that were in Grand Rapids yesterday, I saw the PowerPoint from CMS also and I'm curious to learn more about that, but we don't have any plans like that at this time.

Julien Dumoulin-Smith - *UBS - Analyst*

Great, thank you.

Operator

Kit Konolige, BGC.

Kit Konolige - *BGC Partners - Analyst*

On Bluestone, Dave, you talked about making some progress there, and I understand there will be more detail at EEI. Can you just give us a sense of where you stand relative to your comments at the second quarter? You talked about, I think, $650 million of investment to go there and an expectation that you could get to $100 million in earnings. The target was higher than that, and you talked about white space. Can you fill us in on what kind of progress you have made in those terms?

Dave Meador - *DTE Energy Company - EVP, CFO*

I would rather hold that for EEI. We are making a lot of progress in filling in that white space, and continue to get questions about can you grow this beyond the 120. And we have a fair number of balls in the air right now, but the answer is, is it possible, yes. And that's what we are working our way through right now.

Everything we see there, as you know, the amount of gas that is coming out of that Susquehanna County in particular is, I think, a paradigm shift for a lot of people, and so what you're seeing in that whole region, including our assets, is that over time you're going to see pipes filling up. You're going to see expansions happening faster than people thought at Bluestone and at Millennium. And then, there is ongoing opportunity for whether it be laterals tying to that Bluestone pipe or additional gathering system contracts.

So whether it be Southwestern and/or others, I think over time you're going to see us come back with higher investment numbers and higher earnings than we have previously disclosed. That's not -- I don't think you're going to see us change our 2014 numbers, but there is a lot of positive activity in this space right now.

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Kit, this is Peter. I know the $650 million actually is a spend to date. The way we are thinking about it and talking about this now is a go-forward spend. We are looking at $1 billion to $1.3 billion of capital on this segment from 2013 on, and then we will give you an update at EEI in terms of where we're at.

Kit Konolige - *BGC Partners - Analyst*

Sounds good. I will be looking forward to EEI, then. Thank you.

Operator

Mark Barnett, Morningstar Equity Research.

Mark Barnett - *Morningstar - Analyst*

Just a quick question on something smaller that you mentioned, about your cash-flow guidance for the year. You talked about the improvement, I guess, in working capital versus your plan. Is that something that is going to be more of a sustainable or a non-repeatable thing that we shouldn't expect for 2014?

Dave Meador - *DTE Energy Company - EVP, CFO*

I would characterize it as non-repeatable, more of a one-time.

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Yes, Mark, it's related to underrecoveries. We have the PSCR, the GCR. We had some reconciliations around the choice tracker that went away roughly over a year ago. And we had some underrecoveries.

We settled the cases, got them done earlier, so the collection on those underrecoveries started a little earlier. So they were -- we were planning them to bleed a little bit into 2014, but it turns out that they will occur mostly in 2013.

Mark Barnett - *Morningstar - Analyst*

Okay, thanks a lot. Appreciate it.

Operator

Andrew Levi, Avon Capital Advisors.

Andrew Levi - *Avon Capital/Millennium Partners - Analyst*

So just sticking with the gas and the infrastructure, so it sounds like things are moving along quite nicely, maybe a little bit faster than what you had anticipated earlier in the year for the outer years. At what level of whether it's net income or capital opportunities do you start to consider doing an MLP?

Dave Meador - *DTE Energy Company - EVP, CFO*

As you know, we don't have an exact number, and we have said for some time that we needed to get more scale, and it wasn't just more scale on what I had today, but I also feel strongly that I need line of sight to a set of investments.

So as you know, when you set these up, you would have to have a pool of assets that you either currently own that you could drop in over time or a line of -- a good line of sight on investments going out many, many years, not one year or two years, but more than that.

And we are focused right now on the development side to create that pool of assets, either the assets I have in the ground right now or a line of sight on CapEx for multiple years, and that's where we are putting our time and energy. And over time, we will clarify our thinking on an MLP, but it's too early right now. We just don't have the scale, in our view.

Andrew Levi - *Avon Capital/Millennium Partners - Analyst*

Okay, but I guess it's something that you're working towards, I guess, is what (multiple speakers)

Dave Meador - *DTE Energy Company - EVP, CFO*

Yes, what we are working towards and putting, as I have indicated, our shoulder into is the development side. That is where we are putting all our time and energy and resources to see how we can grow this business and grow it in a high-quality way, as we have done in other segments. It's just not earnings growth for earnings growth sake; we are still trying to stick to our discipline, making sure we have high-quality returns.

Andrew Levi - *Avon Capital/Millennium Partners - Analyst*

That's great. I appreciate it, and go Tigers.

Operator

(Operator Instructions). Matt Tucker, KeyBanc Capital Markets.

Matt Tucker - *KeyBanc Capital Markets - Analyst*

I apologize if you commented on this and I missed it, but there were several media reports earlier this week indicating that you all had reached a deal to sell refining coal to Wisconsin Energy. Would that represent the placement of your eighth REF unit? Are you able to comment on that at all?

Dave Meador - *DTE Energy Company - EVP, CFO*

Normally, we haven't been commenting on the host sites because we're in the middle of placement and negotiations, so usually I would say no. But they pulled an environmental permit, so it was disclosed and that is the eighth unit. And we working on the ninth unit that we hope to have placed and up and running in early 2014.

Matt Tucker - *KeyBanc Capital Markets - Analyst*

Thanks, and what would be the timing on the operations of that eighth unit?

Peter Oleksiak - *DTE Energy Company - SVP Finance*

Like spring.

Dave Meador - *DTE Energy Company - EVP, CFO*

Normally, it's a four- to six-month period to construct, relocate, and then get it up, tested, and up and running. But this is all in line with not only next year's guidance, but our longer-term guidance that we provided for that segment. So these relocations are happening on the right timeline with the right tons of coal, host location, so everything is on track there.

Matt Tucker - *KeyBanc Capital Markets - Analyst*

Okay, great. Thanks for taking my questions.

Operator

Ashar Khan, Visium.

Ashar Khan - *Visium Asset Management - Analyst*

My questions have been answered. Thank you so much.

Dave Meador - *DTE Energy Company - EVP, CFO*

Okay, well, great. And thank you, everybody, for joining us. And again for those of you that will not be at EEI, you can get the webcast presentation on November 12 at 11.15 through our website. And thanks again, and have a great day and a great weekend.

Operator

And with that, once again, ladies and gentlemen, that does conclude today's call. Thank you for your participation and have a great day.