Southern States Utilities

ORIGINAL
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BEFORE THE

FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 950495 - WS

APPLICATION FOR A GENERAL RATE INCREASE

VOLUME I
BOOK 2 OF 22

MINIMUM FILING REQUIREMENTS
PREFILED DIRECT TESTIMONY

Containing

AREND J. SANDBULTE

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DIRECT TESTIMONY OF AREND J. SANDBULTE

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

ON BEHALF OF

SOUTHERN STATES UTILITIES, INC.

DOCKET NO. 950495-WS

Q. **PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A. My name is Arend J. Sandbulte and my business address is Minnesota Power & Light Company (Minnesota Power, MP or the Company), 30 West Superior Street, Duluth, Minnesota 55802.

Q. **IN WHAT CAPACITY ARE YOU EMPLOYED?**

A. My position is Chairman and Chief Executive Officer of Minnesota Power.

Q. **PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL BACKGROUND AS WELL AS YOUR RESPONSIBILITIES IN YOUR CURRENT POSITION.**

A. I am a 1959 graduate of Iowa State University with a Bachelor of Science degree in Electrical Engineering. I also obtained a Master's degree in Business Administration from the University of Minnesota in 1966. I began my career as a rate engineer with Northern States Power Company in 1959. I moved to Minnesota Power in 1964 where I originally served in a similar capacity. I was promoted to financial assistant in 1965, and to Director of the Budgets and Research Department in 1966. I was named Assistant Vice President - Research and Corporate Planning in 1972 and became Vice President - Corporate Planning in 1974. I was named Vice President and Chief Financial Officer in 1976 and Senior Vice President, Finance and Administration, and Chief Financial Officer in 1978. In 1980 I was named Executive Vice President and Chief Financial Officer, and in 1983 I was appointed to the Chief Operating Officer position in addition to retaining the earlier positions. In 1984 I became President and Chief Operating Officer. In 1988 I was elected President and Chief Executive Officer, and in 1989 was named Chairman of the Board, President and Chief Executive Officer. In May 1995 I relinquished my title of President to my successor.

My primary responsibilities in my current position are to provide overall leadership and direction to the Company and to guide development of appropriate long-range strategic plans. I lead and work with the Minnesota Power Board of Directors and provide guidance to the company's top executive officers in managing the strategic activities assigned to them.

Q. **ARE YOU A MEMBER OF ANY PROFESSIONAL SOCIETIES OR ASSOCIATIONS?**

A. I am a Registered Professional Engineer in the states of Minnesota, North Dakota and Wisconsin and a member of the Institute of Electrical and Electronic Engineers (IEEE).

Q. **ARE YOU A MEMBER OF ANY TRADE ASSOCIATIONS?**

A. I am currently President and member of the board of The Association of Electric Illuminating Companies (AEIC), a 108 year old national association of about 80 electric utilities which deals with engineering/technical issues for the electric utility industry. I was until recently a member of the Board of Directors of the Edison Electric

Institute (EEI), the investor-owned utilities trade association. I also serve as a member of the EEI Policy Committee on Environmental Affairs and am past chairman, dealing with such matters as global warming, electro-magnetic fields and other environmentally related issues. I was also until recently a member of the Governmental Affairs Committee of EEI. I am also a board member and past president of the North Central Electric Association (NCEA), a regional electric utility association dealing with various issues facing electric utilities in the midwest.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE A REGULATORY AGENCY?

A. Yes. I have testified on three occasions before the Florida Public Service Commission (FPSC) relative to our various water and wastewater operations which are now collectively known as Southern States Utilities, Inc. (SSU). I have testified in every rate case Minnesota Power has filed since the Minnesota Public Utilities Commission (MPUC) was formed in 1975, including the most recent case which was filed in 1994 (a total of seven different rate cases). I have also testified before the Federal Energy Regulatory Commission (FERC), and its predecessor, the Federal Power Commission. Finally, I have also testified before the Public Service Commission of Wisconsin concerning rates sought by Minnesota Power's Wisconsin utility subsidiary, Superior Water, Light and Power Company.

Generally, I have testified in matters of overall Company policy, as well as rate design, rate of return and similar matters. I have also testified before several other Minnesota regulatory agencies on matters of power plant siting, certificates of need and transmission line routing.

Q. **WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

A. The purpose of my testimony is to provide an overview of Minnesota Power's investment in SSU, to summarize shareholder concerns about that investment, and to confirm that our ability to continue to commit funds to SSU is based to a large degree on receiving fair, reasonable and timely rate relief. Provided this goal is met for Minnesota Power and its investors, we can and will continue to provide financial support necessary for facilities upgrades and the continued superior level of service that SSU customers have begun to expect.

Q. **PLEASE DESCRIBE MINNESOTA POWER'S OWNERSHIP IN SSU.**

A. Minnesota Power owns 100% of Topeka Group, Inc. (Topeka) which in turn owns 100% of SSU. Minnesota Power's equity investment in SSU at year-end 1994 was $78 million, roughly 14% of Minnesota Power's consolidated common equity of $562 million as of the same date. Minnesota Power is a publicly owned Minnesota corporation whose stock is traded on the New York Stock Exchange.

It is important to understand that while SSU does not have any publicly traded shares, it does receive considerable attention from Minnesota Power shareholders, investment analysts and securities rating agencies because of its significance to the consolidated or overall Minnesota Power operations.

Q. **HOW WOULD YOU CHARACTERIZE THE RETURNS EARNED BY SSU FROM THE PERSPECTIVE OF THE MINNESOTA POWER SHAREHOLDER?**

A. The opinion of Minnesota Power shareholders of the returns we have been experiencing from our investment in SSU has been similar to the opinions rendered by the securities rating agencies and analysts who rate and critique Minnesota Power's securities.

One of my duties is to meet with the securities rating agencies such as Standard & Poor's and Moody's. As indicated in Exhibit ___ (AJS-1), Exhibit _____ (AJS-2) and Exhibit _____ (AJS-3), the agencies have continually indicated that our Florida water operations' performance has been "sluggish," "lagging" and inadequate. I also frequently meet with and review reports of investment analyst professionals who similarly indicate their disappointment with our water and wastewater results and look forward to rate relief. Copies of several of these reports are included in Exhibit ____ (AJS-4), Exhibit ____ (AJS-5) and Exhibit ____ (AJS-6).

Q. **WHY SHOULD SSU'S CUSTOMERS BE CONCERNED ABOUT THE RETURN EARNED BY MINNESOTA POWER'S**

SHAREHOLDERS?

A. Customers will be adversely impacted if SSU's access to capital diminishes or its cost of capital increases.

The impact can be expected to follow the course outlined in Dr. Morin's pre-filed direct testimony. Dr. Morin explains that if shareholders do not believe that the authorized return on equity is sufficient to reflect the risk of their investment in SSU, they will be less inclined to purchase Minnesota Power's stock and more inclined to direct Minnesota Power's management to forego further equity investment in SSU. The ultimate effect of these shareholder reactions will be to force SSU to rely more on debt financing to meet its capital needs. A need to resort to debt financing is made more pressing given SSU's limited retained earnings as a result of poor past financial performance. As SSU relies more on debt financing, SSU's capital structure will become more leveraged, and, as noted by Dr. Morin, SSU's future cost of debt will rise, adversely affecting customer rates. As leverage and debt costs rise, Minnesota Power shareholders will face even greater uncertainty about future dividends and earnings from SSU. Ultimately, according to Dr. Morin, to ensure that SSU has continued access to capital to meets its needs, equity investors will require even higher rates of return, again adversely affecting customer rates.

In addition to the customer benefits of a strong equity base for debt financings and capital program funding, supportive MP investors and management have historically provided:

1. Financial guarantees necessary to obtain borrowed funds that would be otherwise unobtainable or obtainable only at a significantly higher cost. Credit support in the form of subordination agreements, continuing ownership covenants, and collateral pledge agreements has also been provided on various SSU obligations.
2. Consolidated insurance coverages with Minnesota Power policies, at significant savings to SSU.
3. Other non-invoiced benefits, such as access to proven human resource, training, audit and safety policies programs and personnel, as outlined in Mr. Vierima's direct testimony.

Q. **HOW IS THE HIGH ENVIRONMENTAL COMPLIANCE CAPITAL SPENDING PROGRAM OF SSU RELATED TO INVESTOR RETURNS?**

A. Any capital invested which is not included in a rate proceeding will have an immediate effect of lowering the utility's return on equity invested in such facilities. As SSU's witnesses will demonstrate, SSU has invested an annual average of $24 million in utility facilities primarily to comply with applicable laws and standards. This is a significant level of capital investment for a utility the size of SSU. To put this in perspective, SSU is investing $24 million in plant when equity investment in SSU is $78 million. Minnesota Power is investing $27 million in electric utility operations at a time when Minnesota Power's electric utility equity capital is $257 million. Like SSU's investments to comply with laws such as the Clean Water Act and the Safe Drinking Water Act and resulting regulations, in the 1970's and 1980's Minnesota Power was required to make significant investment in utility facilities to comply with the Clean Air Act. During the period in which these significant investments were being made, Minnesota Power was forced to seek rate relief from state regulators. Although rate increase applications were more frequent than we would have preferred, we believe the timely filing and administration of those proceedings, the use of projected test years, the ability to recover total revenue requirements in one filing and finally, and perhaps most important, the approval of sufficient levels of rate relief by our regulators to reflect our large capital investments enabled us to make prudent investments in utility equipment which ultimately satisfied all environmental requirements.

Q. **WHAT HAVE BEEN THE FINANCIAL COMMITMENTS OF MINNESOTA POWER TO SSU?**

A. The capital expenditures for all SSU plants, from 1992 through 1996, will total $110 million. As Dr. Morin indicates in his direct testimony, relative to the equity investment of $76 million in 1992, this capital requirement was, and continues to be, very substantial. I do not dispute the necessity of SSU's capital investments. These investments are driven principally by environmental requirements and customer growth, and we support these endeavors. However, speaking for our shareholders, returns realized have been lackluster at best. Over the past five years, SSU's earned return on equity from continuing operations has been less than 3%. By any measure, and regardless of the explanations, this has not been an adequate return.

Q. **DO YOU SUPPORT THE 12.25% RETURN ON EQUITY REQUESTED IN THIS PROCEEDING?**

A. Yes. The 12.25% return developed by Dr. Morin is shown to adequately compensate SSU for the risks associated with this industry in general and this operation in particular. The documentation that Mr. Vierima provides on SSU's extensive capital additions since 1992 heightens the concern of receiving adequate compensation for capital invested.

Q. **DOES THIS CONCLUDE YOUR TESTIMONY?**

A. Yes, it does.

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MOODY'S DOWNGRADES MINNESOTA POWER (SR. TO A3) AND SQUARE BUTTE ELECTRIC COOPERATIVE (SR. UNSEC. TO Baa1).

Approximately $633.7 Million of Debt Securities Affected.

New York, <Rating Date Pending> -- Moody's Investors Service is downgrading the credit ratings of Minnesota Power Company (MP), concluding the rating review initiated on January 15, 1995. The rating action is based on continued sluggish performance at MP's water utility and non-regulated operations and the announcement by the company that it plans to acquire ADESA Corporation, an auto auction company. Moody's is also downgrading the rating of Square Butte Electric Cooperative, whose ultimate credit support derives from a power sales agreement with MP. Moody's will continue to maintain a negative outlook on both MP and Square Butte pending an improvement in financial protection measurements at MP.

Ratings downgraded are:

-more-

Minnesota Power Company's first mortgage bonds and secured pollution control bonds to A3 from A2; shelf registration of senior secured debt to (P)A3 from (P)A2; unsecured pollution control bonds to Baa1 from A3; preferred stock to "baa1" from "a2"; and shelf registration for preferred stock to (P)"baa1" from (P)"a2". In addition, Moody's has downgraded the rating on the company's commercial paper to P-2 from P-1.

Square Butte Electric Cooperative's unsecured pollution control bonds to Baa1 from A3.

MP's financial performance continues to be adversely impacted by weak water utility performance exacerbated by a one-time write-off in 1994 of securities investments. In addition, financial protection measures weakened as interest expense increased 19.6% as a result of increased borrowing by paper operations.

MP has signed a definitive merger agreement to acquire ADESA for $160 million. The planned acquisition of ADESA will be funded by the liquidation of almost 60% of MP's $280 million investment portfolio. ADESA, established in 1992, owns and operates 16 automobile auction centers in the US and Canada and provides a wide range of auto related services. Through a separate subsidiary, ADESA also offers financing to purchasers. The risks associated with ADESA include vulnerability to competitive pressures and a level of tangible net worth of less than $45 million. Additionally, the proposed acquisition will substantially alter the risk profile of MP, increasing the percent of non-regulated assets from 13% to more than 20%.

Minnesota Power is a diversified electric company headquartered in Duluth, Minnesota.

-more-

EXHIBIT_______(AJS-2)

Excerpt - Duff and Phelps Credit Rating Company News Release 3/16/95

CURRENT NEWS

LBJ 14.33 (DJ) D&P, Minn. Power & Light -2-: Affects $670M Debt >MPL

* MPL SOLD * /I RTG *

CHICAGO -DJ- Duff & Phelps Credit Rating Co. downgraded the credit ratings of Minnesota Power & Light Co.'s (MPL) first mortgage bonds and collateralized PCRB's to Single-A-Minus from Single-A, preferred stock to Triple-B-Plus from Single-A-Minus and commercial paper to D-1-Minus from D-1, affecting about $670 million of debt and preferred stock.

The securities are removed from Rating Watch-Down where they were placed on Jan. 12, 1995, said D&P.

D&P attributed the downgrade to Minnesota P&L's changing financial fundamentals and risk profile. Expected improvement in credit protection measures has not materialized, a reflection of the still lagging financial performance of the water utility operations in Florida and the Carolinas, weaker investment portfolio performance, the stagnant electric service territory economy and previously depressed paper prices which negatively impacted the company's investments in that industry.

Additionally, the partial liquidation of Minnesota P&L's investment portfolio to fund the planned acquisition of Adesa Corp. (SOLD), an auto auction company, will reduce liquidity and lower portfolio interest income near term.

/N/C/LBJ/2 (RETURN=next page,DELETE for new request)

EXHIBIT_______(AJS-3)

Excerpt - Duff and Phelps
Credit Rating Company
News Release
1/12/95

MPL - 24 5-8 (N) 13.53 DN 0 5-8 V 268 PAGE 1 OF 2
AI 13.37 (DJ) D&P/Minnesota Power & Light -2:$670M Debt, Pfd Stk Affected

* MPL * /I BON RTG *

NEW YORK -DJ- Duff & Phelps Credit Rating Co. said it has placed the ratings of Minnesota Power & Light Co. (MPL) on Rating Watch-Down.

Minnesota P&L's first mortgage bonds and collateralized pollution control revenue bonds, or PCRBs, are rated Single-A and the preferred stock Single-A-Minus, D&P said, adding that about $670 million of debt and preferred stock is affected.

D&P said: ''(Minnesota P&L) recently announced a plan to acquire an 80% interest in Adesa Corp. (SOLD), an owner and operator of used-car auctions, for about $162 million, which would equal about 30% of (Minnesota P&L)'s common equity. (Minnesota P&L)'s initial investment in Adesa Corp. is expected to be financed through internal funds. If the acquisition is consummated, it would further diversify (Minnesota P&L)'s business interests and likely increase its risk profile.

''Adesa Corp. would become a subsidiary of (Minnesota P&L) as a result of the cash acquisition. The two-year-old Adesa Corp. owns and operates 16 auto-auction facilities in the United States and Canada, making it the third-largest auto auction company in North America. Adesa Corp. is expected to continue its expansion strategy through acquisition of additional independent

MPL/N/AI/2 {RETURN=next page,DELETE for new request}

MPL - 24 5-8 (N) 13.53 DN 0 5-8 V 268 PAGE 2 OF 2
AI 13.37 (DJ) D&P/Minnesota Power & Light -2:$670M Debt, Pfd Stk Affected
(CONTINUED)
auctions. For the 12 months ended Sept. 30, 1994, Adesa Corp. had net income of $7.7 million on revenues of about $87 million.

''(Minnesota P&L) has sizable investments in non-regulated businesses that include paper manufacturing, coal mining and an investment portfolio. (Minnesota P&L) also has regulated water businesses with holdings in Florida, North Carolina, and South Carolina. Regulatory support for these businesses is uncertain; rate increases in Florida and North Carolina have not allowed adequate returns.

''Minnesota Power & Light Co.'s utility operations provide service to northeastern Minnesota and parts of Wisconsin,'' the rating agency said.

(END) DOW JONES NEWS 01-12-95
1:37 PM

MPL/N/ {RETURN for headlines, DELETE for new request}

RESEARCH COMMNTS/INFO/LSTS/OTHR PG 07 OF 12
FAVORABLY POSITIONS IT TO MAINTAIN LARGE COMMERCIAL AND INDUSTRIAL CUSTOMERS OVER THE LONG TERM.

* LIMITED NEED FOR EXTERNAL FINANCING. MPL'S CAPITAL EXPENDITURE BUDGET FOR THE FORESEEABLE FUTURE APPEARS MANAGEABLE. THE UTILITY CONSTRUCTION BUDGET FOR THE PERIOD 1994 THROUGH 1998 TOTALS $334 MILLION, VIRTUALLY ALL OF WHICH TH COMPANY ESTIMATES CAN BE INTERNALLY FINANCED. LIMITED NEED FOR EXTERNAL FINANCING REDUCES THE COMPANY'S EXPOSURE TO THE REGULATORY PROCESS DURING THIS PERIOD.

* NONNUCLEAR FUEL MIX WITH LIMITED EXPOSURE TO CLEAN AIR ACT AMENDMENTS (CAAA). MPL'S ELECTRIC FUEL MIX CONTAINS NO NUCLEAR GENERATION. THE UTILITY DOES NOT EXPECT TO BE SIGNIFICANTLY IMPACTED UNDER PHASE I OF THE CAAA, AS ITS GENERATING UNITS BURN MAINLY LOW SULFUR COAL AND ARE EQUIPPED WITH POLLUTION CONTROL DEVICES. THE COMPANY EXPECTS TO MEET PHASE II EMISSIONS LIMITS, EFFECTIVE JANUARY 1, 2000, THROUGH FUEL SWITCHING AND THE INCREASED USE OF SCRUBBERS THE IMPACT OF COMPLIANCE ON ANNUAL REVENUE REQUIREMENTS IS LIKELY TO BE MODEST.

INVESTMENT CONCERNS:

*PROPOSED ACQUISITION OF ADESA, AN AUTO AUCTION BUSINESS.

RLST AID CONT 01/09/95 11:14

RESEARCH COMMNTS/INFO/LSTS/OTHR PG 08 OF 12
*ABOVE-INDUSTRY AVERAGE EARNINGS PAYOUT RATIO COULD LEAD TO BELOW AVERAGE NEAR TERM DIVIDEND GROWTH. MPL'S CURRENT ANNUAL DIVIDEND OF $2.02 REPRESENTS AN 99% PAYOUT OF OUR ESTIMATED 1994 EPS OF $2.05 VERSUS THE INDUSTRY AVERAGE OF ABOUT 78%. THE PAYOUT OF BOOK VALUE AT DEC. 31, 1993 WAS 10.1% VERSUS THE INDUSTRY AVERAGE OF ABOUT 9.3%. GIVEN LIMITED EXPECTATIONS FOR SIGNIFICANT EARNINGS GRWOTH AT THE ELECTRIC UTILITY, FUTURE DIVIDEND GROWTH WILL BE DEPENDENT ON IMPROVED EARNINGS AT THE WATER UTILITIES AND UTILTY RELATED BUSINESS.

*NEAR-TERM EARNINGS GROWTH DEPENDS ON CONTINUED REASONABLE RATE REGULATION FOR THE WATER UTILITIES. SINCE 1984 WHEN MPL ENTERED THE WATER UTILITY BUSINESS, THE COMPANY HAS UPGRADED EXISTING OPERATIONS AND BUILT NEW FACILITIES. THE WATER OPERATIONS REPORTED A PROFIT FOR 1993 VS A LOSS IN 1992, DUE TO RATE RELIEF AUTHORIZED BY THE REGULATORS IN FLORIDA AND THE CAROLINAS TO RECOVER THESE INVESTMENTS. HOWEVER, IN ORDER TO BRING THE RATE OF RETURN ON INVESTMENTS IN THE WATER UTILITIES UP TO A TYPIPCAL UTILITY LEVEL, ADDITIONAL RATE RELIEF WILL BE REQUIRED WITHIN THE NEXT YEAR OR TWO.

* ELECTRIC CUSTOMER MIX HEAVILY WEIGHTED TOWARD INDUSTRIAL. MPL'S INDUSTRIAL CUSTOMER BASE ACCOUNTED FOR 62% RETAIL ELECTRIC REVENUES IN 1993, WELL ABOVE THE INDUSTRY AVERAGE OF ABOUT 25%. ELECTRIC SALES TO THE INDUSTRIAL SECTOR ARE GENERALLY MORE VOLATILE THAN SALES TO THE COMMERCIAL OR RESIDENTIAL SECTORS DUE TO THE SUSCEPTIBIILITY OF THESE CUSTOMERS TO ECONOMIC DOWNTURNS IN THE
RLST AID CONT 01/09/95 11:14

EXHIBIT_______(AJS-5)

Excerpt - Oppenheimer & Co.
Research Comments
1/13/95

Craig Lucas
Oppenheimer & Co
1/13/95

Company	Date	Model Rank	1/12/95 Closing	1994E EPS	1995E EPS	1994E P/B	1995E P/E
MPL	1/25/95	M	24.625	1.82	1.88	1.23	13.1

Dividend maintenance likely.

After review, we are lowering our 1994 earnings estimate to $1.82 our 1995 estimate to $1.88. Our 1996 estimate is $2.22. With long term earnings power of $2.20, the stock appears fairly valued at current prices. However, a near term earnings crunch, coupled with lingering uncertainty regarding the non-utility operations (in particular Adesa and the water utility), is likely to result in continued price weakness. Compounding the problem, with a forecast 1995 payout of 107%, a dividend cut remains a possibility. As such we consider the stock untimely and fairly valued at $23.00

We expect MPL's core utility operations to earn $1.19 on a book of $9.91 (12% ROE) in 1994, earn $1.14 in 1995 (11.5% ROE) and earn $1.14 in 1996 (11.6% ROE).

MPL's portfolio subsidiary took a $10 million write-off in the first quarter of 1994 and is expected to post only $0.20 of earnings on $7.20 of book (3% ROE). In 1995 MPL will use $162 million of equity from the portfolio to close on the purchase of Adesa. The portfolio should contribute $0.14 in 1995 (3.33% ROE) and $0.05 in 1996 (4% ROE). Assuming Adesa is ultimately acquired, we forecast earnings of $0.11 in 1995 on book of $0.29 (2% ROE) and earnings of $0.42 in 1996 (7.14% ROE).

The Lehigh Acquisition (land being sold-off in Florida) will contribute $0.34 on a book of $0.63 (56% ROE) in 1994, and should continue to earn strong returns prospectively ($0.23 in 1995 and $0.20 in 1996).

We expect water utility operations to contribute $0.06 in 1994 on a book of $2.17 (2.59% ROE), contribute $0.15 in 1995 (5.0% ROE), and earn $0.21 in 1996 (7% ROE). <u>The water unit earns a sub-par return on equity because of rate base disallowances due to used-and-useful issues. A rate case in 1995 may resolve these issues.</u>

BNI coal should continue contributing $0.11 per share (1994 book $0.43, 26% ROE). Minnesota Paper should earn $0.03 in 1994 on a book of $1.07 (2.5% ROE), and continue to earn $0.03 prospectively. Rendfield equipment will continue to be a $0.04 drag to earnings and Rainy River should be earnings neutral. Recycled Fiber operations will contribute $0.02 prospectively (1994 book $1.06, 2% ROE). Corporate overhead is expected to be a $0.15 drag in 1994 and prospectively.

WR	1/25/95	O	29.25	2.56	2.54	1.22	11.5

EXHIBIT_______(AJS-6)

Excerpt - Donaldson, Lufkin Research Comments 3/3/95

TO: Kim Lindstrom

DONALDSON, LUFKIN & JENRETTE
March 3, 1995

James L. Dobson, CFA (212) 504-2614
Aarti Verma (212) 504-4252

MINNESOTA POWER & LIGHT (MPL: $25 3/4)

Recent Visit with Management Leaves Us (Again) Unconvinced in ADESA Transaction's Strengths; *Maintain Underperform Rating and Estimates.*

Range:		Earnings Per Share				
$30 - $24		Old	New	P/E Ratios	Quarterly EPS Est.	% Chg.
(FY:Dec.)	1996E	$2.40		10.7	F1Q $0.51A vs. 0.64A	-20.3%
	1995E	2.20		11.7	F2Q 0.44A vs. 0.46A	-4.3%
	1994A	1.92		13.4	F3Q 0.51A vs. 0.61A	-16.4%
	1993A	2.20		11.7	F4Q 0.46A vs. 0.49A	-6.1%

Yield: 7.9%
Dividend: $2.04
Market Cap.: $804
Avg. Trading Vol.(000): 36
5-Yr. Growth Rate: 2.3%
Book Value: $20.78

RATING: Underperform   Change: None

VIEWPOINT

Minnesota Power & Light (MPL) currently trades at 11.7 times our 1995 earnings estimate, 1.2 times 1994 book value and a current yield of 7.9%. This compares with DLJ Electric Utility Universe averages of 10.7x, 1.3x and 7.1%, respectively. Our valuation model for MPL is based on no dividend growth over the next three years, 1.9% annually thereafter and a discount rate of 10%. This suggests a fair value for MPL of $23 per share versus a current price closer to $26. Due to the high dividend payout ratio, erratic earnings stream and apparent overvaluation, we are maintaining our *underperform* rating.

IMPORTANT POINTS

Recently, we had an opportunity to visit with the management of MPL in New York. Despite management's continued optimism for the company's recently announced purchase of an 80% stake in the ADESA Corporation, we remain unconvinced that management's optimistic expectations will be met. ADESA owns and operates automobile auctions in the U.S. and Canada, through which used cars and other vehicles are sold to franchised automobile dealers and licensed used car dealers. MPL management expects that ADESA can double the number of auctions it currently owns, while more than doubling revenues and earnings. More than half of the growth is expected to come from acquisitions. Although the prospects for the auto auctioning business are better than the electric utility business, it appears that management is relying on little competition from the other large participants in the auto auctioning business to accomplish a significant number of small acquisitions at attractive prices. Without this, management suggested it would be harder to reach their expansion goals. Returns in the first few years are likely to be about 5%.

We continue to expect the company will file a rate case in Florida for its water utility subsidiaries in 1995. Smaller than expected rate increases for this subsidiary have prevented it from growing beyond a single digit return on equity. Admittedly, a successful outcome in the next case could put the subsidiary on track to earning a better return in Florida. Separately, MPL continues to look for additional water properties to continue to expand this segment of their business.

With the recent rate increase at its electric utility business in Minnesota, earnings from this segment should improve modestly in 1995. Further, the company's paper business should also provide some upward pressure to earnings in 1995, due to better paper prices recently. We are maintaining our earnings estimates of $2.20 and