# Enron Corp.

Company Update

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**Rating: STRONG BUY *(Moderate Risk)***

- Enron left analysts and investors "giddy" after recent conference, highlighting telecommunications and wholesale energy.
- Raising price target to $85 based on revised sum-of-the-parts model to include telecom.
- Upholding Strong Buy rating on ENE.

ENE (71 5/8)—NYSE

January 25, 2000

| | Earnings Per Share Fiscal Year Ending | | | P/E | Ind. | | Shares O/S | 52-Week |
|---|---|---|---|---|---|---|---|---|
| | 12/98 | 12/99 | 12/00E | 12/00E | Div. | Yield | (Mil.) | Range |
| **New** | **$1.00** | **$1.18** | **$1.37** | **52.3X** | **$0.50** | **0.7%** | **779.1** | **67-30** |
| **Old** | | | | | | | | |

DJIA: 11,251.70

S&P 500: 1441.36

PSI Natural Gas Pipelines Index: 991.35

Priced as of the close, January 21, 2000.

Note: A PSI index's market-cap-weighted performance is on a total-return basis and, in most instances, from 1979. Most Prudential Securities Incorporated indexes (for about 200 industries in 12 economic sectors) are also segmented by small-, mid-, and large-cap stocks. For more information regarding these indexes and their composition please contact your Prudential Securities representative. Prudential Securities research is also available on Bloomberg, First Call/Research Direct, and Multex.

## *Enron Conference Focused On Opportunities In Leveraging Services Off Existing Energy And Communications Networks*

*Enron Corp. is a leading integrated natural gas and electric company, with both U.S. and international operations. The company owns about $30 billion in assets, produces electricity and natural gas, and develops, constructs, and operates worldwide energy and water facilities. It is also a leader in the marketing and risk management of energy commodities and financial services worldwide.*

At its comprehensive financial analysts conference held in Houston on January 20, Enron Corp. highlighted its expanding role as a market leader in growth opportunities foreseen in the global wholesale energy business, its growing profitability in retail energy services, and its expanding role in broadband network applications. While these have been central growth themes at Enron, the new news at this year's conference was the introduction of its communications business model and targeted market share, highlighted by the announcement of a joint marketing agreement with Sun Microsystems to expand its broadband Internet services. Unique to Enron's communications strategy is its approach to creating a high-quality, flexible network that can differentiate the quality of service.

**Enron Appears Undervalued On A Sum-Of-Its-Parts Basis.** Management told an impressive story at its conference, and articulated the economics of its broadband services and retail energy services (Enron Energy Services, or EES) businesses. Based on a 20% share of the bandwidth intermediation market (bandwidth management, trading, finance) and a 10% share of the content services market (streaming, data management, storage), Enron Broadband could have a present value of more than $30 billion. Enron Energy Services turned profitable in the first quarter, and management has raised

## *Figure 1. Enron Corp. Net Asset Valuation*

(Dollars in millions, except per share amounts)

| | | Factor | | Total Value | |
|---|---|---|---|---|---|
| | | | | ($Mil) | Per Share |
| **Gas Transmission** | | | | | |
| 2000E Operating Income | $383.0 | | | | |
| DD&A | 110.0 | | | | |
| 2000E EBITDA | $493.0 | | 10.0 X | $4,930.0 | $6.40 |
| **Portland General** | | | | $1,900.0 | $2.47 |
| **Enron Wholesale** | | | | | |
| 2000E Operating Income | $1,566.0 | | | | |
| DD&A | $190.0 | | | | |
| 2000E EBITDA | $1,756.0 | | 20.0 X | $35,120.0 | $45.61 |
| **Azurix Water** | | | | | |
| Market Price (per share) | $10 | | | | |
| Shares Outstanding (Mil.) | 117 | | | | |
| ENE % Ownership | | | 68% | $796.3 | $1.03 |
| **ENE Broadband (Communications)** | | | | | |
| Bandwidth Intermediation | | | | | |
| 2004 Operating Income | $1,000 | | | | |
| Valued at 20x, discounted @11% | | 20 | 11% | $14,000.0 | $18.18 |
| Content Services | | | | | |
| 2008 Operating Income | $1,000 | | | | |
| Valued at 20x, discounted @17% | | 20 | 11% | $18,000.0 | $23.38 |
| Less G&A | | | | $3,000.0 | |
| **Total Broadband Services** | | | | $29,000.0 | $37.66 |
| **Total Core Asset Value** | | | | **$71,746.3** | **$93.18** |
| **Adjusted For:** | | | | | |
| **Working Capital (a/o 9/30/99)** | | | | $898.0 | $1.17 |
| **Long Term Debt (a/o 9/30/99)** | | | | ($8,592.0) | ($11.16) |
| **Total Core Asset Value** | | | | **$64,052.3** | **$83.18** |
| **Enron Energy Services** | | | | | |
| **2000 Operating Profit** | $75.0 | | 20.0 X | $1,500.0 | $1.95 |
| **Total Net Asset Value** | | | | **$65,552.3** | **$85.13** |

Source: Company information and Prudential Securities estimates.

its projections for annual EBIT in 2000 to $75 million. We have assessed a value of about $37 per share (of which $17 is incremental) for Enron's expanded broadband (communications) business, a conservative value of $1.95 for its growing retail energy services, and have added $14 in 2000 EBITDA estimates and working capital adjustments. Thus, we are raising our 12-month price target to $85 from $52 per share on a revised sum-of-the-parts valuation of the company's individual business units. While we admit that at a multiple of 62 times 2000 estimated earnings our price target appears strong, our sum-of-the-parts valuation methodology has proved to be an excellent barometer of Enron's stock performance over the past year. Despite its recent stock price surge, we continue to uphold a Strong Buy rating, anticipating 25% upside in capital appreciation.

**Enron's Low-Cost Fiber Network Should Create Inherent Shareholder Value In Providing Differentiated Services.** Enron's expanded communications effort has captured a great deal of attention from Wall Street with the increasing popularity of Internet stocks. However, Enron believes that the existing Internet platform will not be capable of handling the anticipated broadband exploration as it was designed for the "test world." Enron's approach is to build a global fiber-optic network of up to 18,000 route miles of which about 12,325 route miles are in place, that will able to handle the highest bandwidth applications.

The "Enron Intelligent Network" will use fiber, servers, pooling points, and software to deploy an open, efficient system at low capital requirements. It plans to connect more than 200 cities in 2000, including the U.S. and international markets. In partnership with both Sun Microsystems and Compaq, Enron plans to develop a distributed server and computer architecture that will enhance storage and simultaneous streams. Enron's goal is to connect as many switches (using Lucent hardware) and servers (Sun Microsystems) as possible, and will use public pooling points (NYC, L.A., London) and install its own pooling points to gain access to all network systems on a real-time basis.

Two cash flow streams are likely to be generated from bandwidth intermediation and content services. As part of its bandwidth intermediation strategy, Enron plans to manage bandwidth and differentiate between high- and low-quality bandwidth. Enron also plans to standardize bandwidth trading, and offer structured finance and risk management services to its customers. Enron's content services focus will be on video streaming and rich media, for which we believe demand is increasing, and other customized services. It should allow customers to select a certain level of service quality, and would charge on a metered usage basis rather than a dedicated network basis.

While one might ask how an energy company can compete in the Internet world, Enron's answer is that the business parallels the gas and electricity industry, where Enron is a market leader. Also, Enron has hired highly skilled personnel from the telecommunications industry and has formed strategic alliances with Sun Microsystems, Lucent Technologies, Cisco Systems, Ciena, RealNetwork, and Broadband. In its just-announced agreement with Sun, Enron plans to build out the footprint of its broadband infrastructure and software, using the Sun platform. As part of the buildout, Enron will likely purchase 18,000 servers and storage services from Sun, and in turn, plans to sell broadband video streaming services to Sun's worldwide operations. This partnership is a major endorsement of Enron's broadband capabilities, technology, and expertise.

Strategically, we believe Enron is way out in front of its competition not only in its core wholesale gas and power businesses but also in its evolving retail services unit. At the conference, management positioned the company as a network of assets and capabilities, differentiating itself from its energy peers. Enron emphasized its continued strong growth in its wholesale energy business, both in the U.S. and overseas, and stressed the turning point for its retail energy services business with its fourth-quarter profitability. In its wholesale energy business, growth in the European markets is expected to continue to be exponential in gas and power marketing sales. The retail energy marketing division, EES, should double the revenues under contract in 2000 to at least $16 billion, of which $1.2 billion has already been signed this month. Enron's burgeoning communications effort should start to contribute to earnings in 2000 in its bandwidth intermediation services segment. This year is also likely to be a transitional one as Enron focuses on improving its returns on invested capital. It expects to close the already-announced sales of Portland General in the third quarter.

**Ownership Of Gas Pipelines Produces Stable Returns And Improves Credit Quality.** While we once thought Enron would spin off its unregulated gas pipelines into a master limited partnership structure, we now believe that Enron will retain its pipelines for the high returns on invested capital and substantial cash flows. Enron continues to emphasize that its gas pipeline business is still part of its core strategy. Enron's pipeline system is characterized by a low-cost system that serves the California, Midwest, and Florida markets where significant new gas-fired power generation is planned.

While future capital expenditures are likely to approximate depreciation and amortization expense, planned expansion of the 50%-owned Florida Gas Transmission system, and the recently completed cross-border Northern Border pipeline should add incremental earnings in 2000. Since its completion, Northern Border has been running full at 2.4 bcf/d, despite concerns that Canadian gas supply may not be sufficient to fill the pipeline's transportation capacity, and another $90 million expansion is in the works. The Northern Natural pipeline, which generates more than 50% of segment income, should benefit from a 1999 rate settlement that improved its competitive position in its southern markets.

**Wholesale Energy Markets In North America Expanding With Deregulation And E-Commerce.** In North America, Enron is the established leader in gas and power marketing. It is expanding its presence in trading coal, weather derivatives, crude, pulp, and paper products and is building its energy network in both North America and Europe. With people and systems in place, Enron's incremental cost to enter new markets is relatively low. It is building an enormous merchant platform on which to leverage its commodity sales and asset-based capabilities.

The wholesale energy market is growing at an annual rate at the upper end of the 35%-40% range, as the ownership of generating plants is shifting from electric utilities to non-traditional energy service providers. Many of these new players may own the power assets under unregulated, "at-risk" structures. Electricity price volatility is also likely to increase, and strict environmental issues will expose a tremendous number of electric generating plants to extensive capital upgrades. Moreover, Enron's expansion into e-commerce or online marketing should increase its trading volumes in all energy commodities. All of these changes should offer opportunities for Enron Wholesale to provide new products and services.

**Growth In European Gas And Power Marketing Resembles That Of The U.S. Four To Five Years Ago...** Key to the future growth story at Enron Wholesale is its entry into the European markets. On the heels of deregulation and privatization, we believe the European market is evolving at a more rapid pace than in the U.S., and the gas and power marketing landscape is basically virgin territory. Assuming this market develops at a pace at least comparable to that of the U.S. markets, it should offer potential exponential returns over the next 2-3 years. Enron has applied its energy network business model to the U.K., continental Europe, and the Nordic region. The U.K. gas market has been open to competition since 1996, and the power market was fully deregulated in May 1999. In the U.K. alone, the total wholesale gas and power market is about $17 billion in annual revenues, and in our view, Enron has already established a strong asset base and marketing presence.

**…And Accelerated Earnings and Growth Opportunities Extend Into Continental Europe.** In continental Europe, opportunities are even greater. The total market size is about $156 million in annual revenues, almost 10 times larger than the U.K. market. Enron is extending its energy network through coal, gas, and oil-fired power plant development and sourcing and moving power within and between the countries. Enron is participating in all major markets, and targeted countries include Italy, Germany, Switzerland, Holland, Belgium, and the Czech Republic. Power volumes and transactions have grown at exponential rates. In 1999, volumes increased to 7,201 thousand megawatt hours from 186 thousand MWh in 1998, and the number of transactions increased to 8,859 from 414.

**Enron Online Creates Opportunity To Grow Volumes And Expand Business.** Rolled out in November 1999, Enron Online has already begun to contribute to incremental growth in wholesale marketing volumes. It is also serving as a mechanism to increase Enron's global reach in energy trading. Cumulative transactions to date total more than 10,000, representing 18% of global volumes and 27% of transactions. Enron Online competes in the business-to-business market, and major competitors include Cisco Online, FreeMarkets, and Altrade. What differentiates Enron is that its Web-based service is free to its users, and it offers real-time transactions and customer viewing rather than "matched" transactions. Barriers to entry include extensive global due diligence requirements and experienced traders. Excluding personnel requirements, Enron's investment in Enron Online is about $15 million.

**Reducing Capital Intensity In Global Power Development.** Enron is shifting its international strategy from one of capital intensity to the recurring theme of leveraging its merchant services off of its energy network base. During the 1993-98 time period, Enron's international strategy was focused on establishing asset positions primarily through the development of power plants and pipelines systems in South America, Asia, and Australia. From 1998 to date, Enron focused on global expansion, and going forward, plans to focus on providing value-added merchant services. In Australia, Enron plans to leverage its "network effect" by offering coal trading (Australia is the leading global coal exporter), weather trading, and Enron Online services. Japan represents enormous growth opportunities in gas and broad product offerings, and South Korea is beginning to open its power markets. The Southern Cone of South America and India remain a core focus, where Enron has an established asset network, and the Caribbean may afford global liquid natural gas (LNG) opportunities.

**After Turning EBIT Positive In The 1999 Fourth Quarter, EES Could Generate Significant EBIT In 2000.** In the fourth-quarter 1999, EES generated $7 million in earnings, above our forecast of $1 million, marking the first quarter the segment was profitable. For the full year, Energy Services still reported a loss of $68 million, but now that the segment has turned the corner, it should generate significant profits in 2000. In 1999, EES signed contracts with a total value of $8.5 billion, a 125% increase over 1998 and about $500 million over budget, and plans to sign another $16 million in 2000, including European customers.

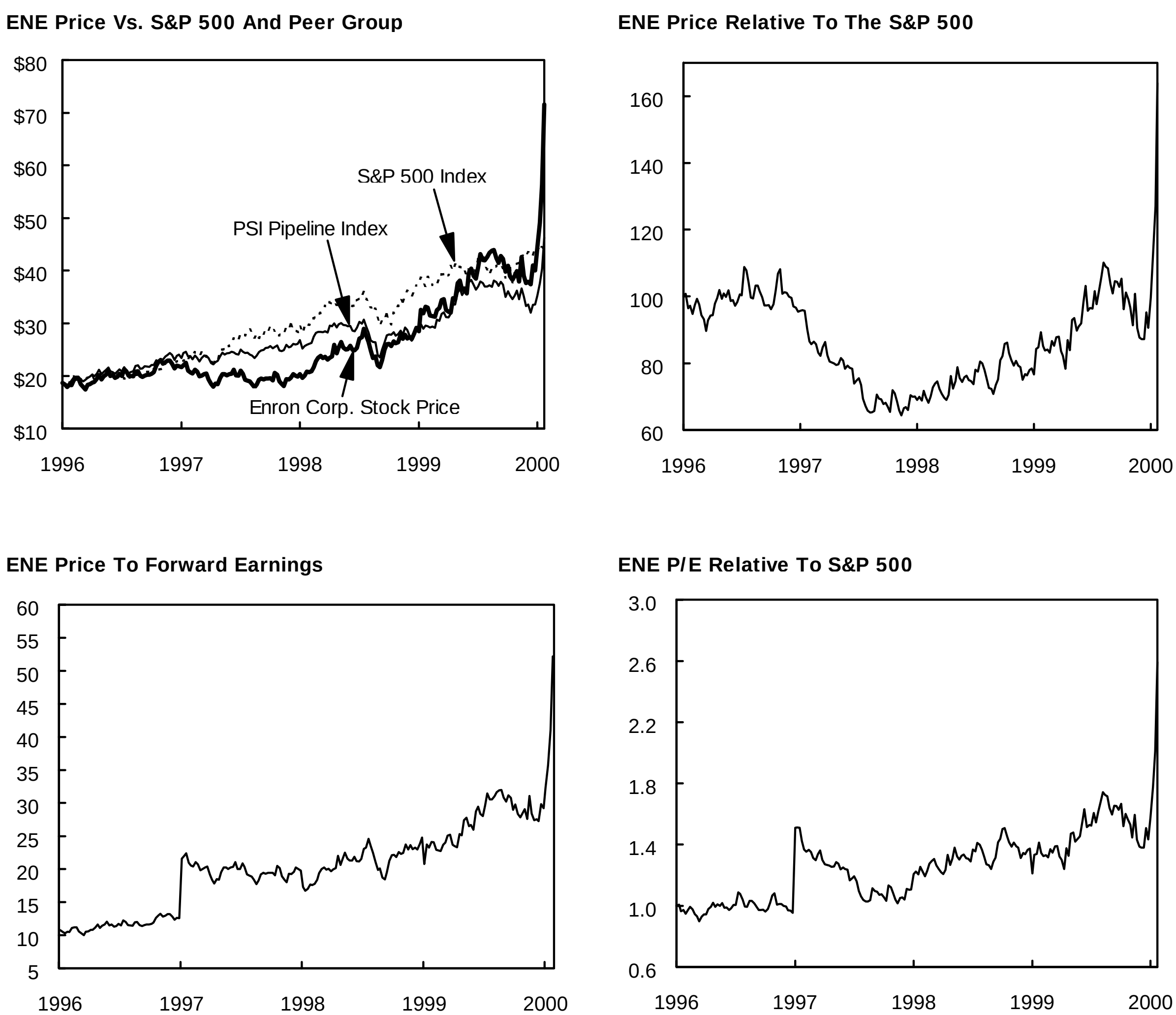
Under ten-year average contracts, EES offers an array of energy services that create value through economies of scale, reduced cost of sales, improved execution through engineering expertise, and access to capital and risk management. In a "margin stacking" concept, EES builds value (or yield) by adding services (and margin) under each contract such as installing energy-efficient equipment, packaging energy needs, wireless meter reading, and outsourcing O&M, for example. A typical contract at

Enron is primarily commodity-based, which carries lower margins, but EES plans to increase its returns as it increases outsourcing services and reduces the commodity portion of its contracts to 50%.

**A Quick Look At Fourth-Quarter EPS, In Line With Expectations.** Adjusted for offsetting minor gains and losses, Enron Corp. reported fourth-quarter earnings of $0.31 per share, up $0.07, or 29% from the same period last year. Full-year 1999 diluted earnings, adjusted for non-recurring charges, were $1.18 per share versus $1.00 for 1998. One-time items in the quarter included a $16 million pretax gain on the sale of certain power-generation facilities at Portland General, offset by a $20 million loss on restructuring charges at subsidiary, Azurix, Inc.

Overall, pretax earnings were about 12% below our expectations, with the majority of the disappointment in Enron's Energy Asset & Investment segment. Segment earnings of $149 million were 38% below our estimate, partially reflecting fewer asset sales and rationalizations. Also, we believe that Enron's strategic investment portfolio in E&P interests may have underperformed during the quarter. Partially offsetting the disappointment in the Energy Asset segment were better-than-expected results in Enron's regulated gas and electric transmission and distribution businesses and lower interest expenses.

***Figure 2. Enron Corp. Valuation Measures***




Source: Company information and Prudential Securities estimates.

***Figure 3. Enron Corp. Quarterly Income Statement***

(Dollars in millions, except per-share data)

| | 1998 | | | | | 1999 | | | | | 2000E |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1Q | 2Q | 3Q | 4Q | Year | 1Q | 2Q | 3Q | 4Q | Year | Year |
| **Segment Operating Income:** | | | | | | | | | | | |
| Transportation & Distribution | | | | | | | | | | | |
| Gas Pipeline Group | $126.0 | $72.0 | $69.0 | $84.0 | $351.0 | $126.0 | $72.0 | $85.0 | $97.0 | $380.0 | $395.2 |
| Portland General | 79.0 | 62.0 | 61.0 | 84.0 | 286.0 | 92.0 | 56.0 | 52.0 | 89.0 | 289.0 | 290.0 |
| Wholesale Energy Oper. & Svcs. | | | | | | | | | | | |
| Commodity Sales & Service | 129.0 | 23.0 | 152.0 | 107.0 | 411.0 | 224.0 | 81.0 | 172.0 | 151.0 | 628.0 | 754.4 |
| Energy Assets & Investments | 151.0 | 258.0 | 160.0 | 140.0 | 709.0 | 136.0 | 325.0 | 240.0 | 149.0 | 850.0 | 875.0 |
| Unallocated Expenses | (31.0) | (40.0) | (35.0) | (46.0) | (152.0) | (40.0) | (50.0) | (34.0) | (37.0) | (161.0) | (140.0) |
| Exploration & Production | 43.0 | 29.0 | 25.0 | 31.0 | 128.0 | 12.0 | 20.0 | 33.0 | 0.0 | 65.0 | 0.0 |
| Corporate & Other | 1.0 | (16.0) | (4.0) | 26.0 | 7.0 | 14.0 | (9.0) | (23.0) | 21.0 | 3.0 | (70.0) |
| **Total Core EBIT** | **$498.0** | **$388.0** | **$428.0** | **$426.0** | **$1,740.0** | **$564.0** | **$495.0** | **$525.0** | **$470.0** | **$2,054.0** | **$2,224.6** |
| Energy Services | (27.0) | (43.0) | (23.0) | (26.0) | (119.0) | (31.0) | (26.0) | (18.0) | 7.0 | (68.0) | 75.0 |
| **EBIT (before Min. Interest)** | **$471.0** | **$345.0** | **$405.0** | **$400.0** | **$1,621.0** | **$533.0** | **$469.0** | **$507.0** | **$477.0** | **$1,986.0** | **$2,299.6** |
| Net Interest Expense | (133.0) | (131.0) | (134.0) | (152.0) | (550.0) | (175.0) | (175.0) | (187.0) | (119.0) | (656.0) | (700.0) |
| Sub. Pfd. Stock Dividend | (19.0) | (20.0) | (19.0) | (19.0) | (77.0) | (19.0) | (19.0) | (19.0) | (19.0) | (76.0) | (76.0) |
| Enron Oil & Gas | (12.0) | (6.0) | (2.0) | (4.0) | (24.0) | 6.0 | 0.0 | 0.0 | 0.0 | 6.0 | 0.0 |
| Other Minority Interest | (13.0) | (13.0) | (14.0) | (13.0) | (53.0) | (39.0) | (23.0) | (38.0) | (41.0) | (141.0) | (145.6) |
| Total Minority Interest | (25.0) | (19.0) | (16.0) | (17.0) | (77.0) | (33.0) | (23.0) | (38.0) | (41.0) | (135.0) | (145.6) |
| **EBIT** | **$294.0** | **$175.0** | **$236.0** | **$212.0** | **$917.0** | **$306.0** | **$252.0** | **$263.0** | **$298.0** | **$1,119.0** | **$1,378.0** |
| Current | (26.0) | (24.0) | (19.0) | (63.0) | (132.0) | (51.0) | (43.0) | (67.0) | 16.4 | (144.6) | (162.3) |
| Deferred | (54.0) | (6.0) | (49.0) | 22.0 | (87.0) | (2.0) | 13.0 | 27.0 | (50.0) | (12.0) | (40.0) |
| Total Income Taxes | (80.0) | (30.0) | (68.0) | (41.0) | (219.0) | (53.0) | (30.0) | (40.0) | (33.6) | (156.6) | (202.3) |
| Tax Rate | 27.2% | 17.1% | 28.8% | 19.3% | 23.9% | 17.3% | 11.9% | 15.2% | 11.3% | 14.0% | 14.7% |
| Recurring Net Income | 214.0 | 145.0 | 168.0 | 171.0 | 698.0 | 253.0 | 222.0 | 223.0 | 264.4 | 962.4 | 1,175.7 |
| Total Preferred Dividends | (4.0) | (5.0) | (4.0) | (4.0) | (17.0) | (4.0) | (19.0) | (19.0) | (24.0) | (66.0) | (76.0) |
| **Recurring Net to Common** | **$210.0** | **$140.0** | **$164.0** | **$167.0** | **$681.0** | **$249.0** | **$203.0** | **$208.0** | **$244.4** | **$904.4** | **$1,099.7** |
| Nonrecurring / Special Items | 0.0 | 0.0 | 0.0 | 5.0 | 5.0 | (131.0) | 0.0 | (67.0) | (2.6) | (200.6) | 0.0 |
| Net Income to Common | 210.0 | 140.0 | 164.0 | 172.0 | 686.0 | 118.0 | 203.0 | 141.0 | 241.8 | 703.8 | 1,099.7 |
| **Basic EPS:** | | | | | | | | | | | |
| Recurring Earnings | $0.34 | $0.22 | $0.25 | $0.25 | $1.06 | $0.38 | $0.29 | $0.29 | $0.34 | $1.29 | $1.55 |
| Reported Basic Earnings | $0.34 | $0.22 | $0.25 | $0.26 | $1.07 | $0.18 | $0.29 | $0.20 | $0.34 | $1.01 | $1.55 |
| **Diluted EPS:** | | | | | | | | | | | |
| **Recurring Earnings** | **$0.32** | **$0.21** | **$0.24** | **$0.24** | **$1.00** | **$0.34** | **$0.26** | **$0.27** | **$0.31** | **$1.18** | **$1.37** |
| Nonrecurring / Special Items | $0.00 | $0.00 | $0.00 | $0.01 | $0.01 | ($0.18) | $0.00 | ($0.09) | ($0.00) | ($0.26) | $0.00 |
| Reported Diluted Earnings | $0.32 | $0.21 | $0.24 | $0.25 | $1.01 | $0.16 | $0.26 | $0.18 | $0.31 | $1.00 | $1.47 |
| Primary Shares Outstanding | 610.0 | 638.6 | 658.0 | 662.0 | 642.2 | 658.0 | 708.0 | 714.1 | 715.3 | 698.9 | 708.0 |
| Diluted Shares Outstanding | 659.6 | 692.6 | 712.0 | 716.0 | 695.1 | 744.0 | 771.0 | 781.1 | 779.1 | 768.8 | 800.0 |
| Dividends Per Share | $0.12 | $0.12 | $0.12 | $0.12 | $0.48 | $0.12 | $0.12 | $0.12 | $0.13 | $0.50 | $0.53 |
| Book Value | — | — | — | — | $10.66 | — | — | — | — | $11.17 | $12.19 |
| Avg Return On Equity | — | — | — | — | 9.4% | — | — | — | — | 10.5% | 11.3% |
| Return on Total Capital | — | — | — | — | 12.3% | — | — | — | — | 7.5% | 7.8% |

Source: Company information and Prudential Securities estimates.

## *Figure 4. Enron Corp. Annual Income Statement*

(Dollars in millions, except per-share amounts)

| | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000E |
|---|---|---|---|---|---|---|---|---|
| **Segment Operating Income:** | | | | | | | | |
| Transmission & Distribution | | | | | | | | |
| Gas Pipeline Group | $390.2 | $403.1 | $397.8 | $415.8 | $364.0 | $351.0 | $380.0 | $395.2 |
| Portland General | — | — | — | — | 114.0 | 286.0 | 289.0 | 290.0 |
| Wholesale Energy Oper. & Svcs. | | | | | | | | |
| Commodity Sales & Service | — | — | — | — | 249.0 | 411.0 | 628.0 | 754.4 |
| Energy Assets & Investments | — | — | — | — | 565.0 | 709.0 | 850.0 | 875.0 |
| Unallocated Expenses | — | — | — | — | (160.0) | (152.0) | (161.0) | (140.0) |
| Total Wholesale | — | — | — | — | 654.0 | 968.0 | 1,317.0 | 1,609.4 |
| As Previously Reported Prior 1/99) | | | | | | | | |
| Enron Capital & Trade Reso. | 168.8 | 225.1 | 232.5 | 279.6 | 400.0 | 673.4 | 604.3 | 809.4 |
| International | 131.3 | 147.7 | 118.1 | 120.9 | 217.0 | 294.6 | 742.7 | 800.0 |
| Engineering & Construction | 0.0 | 0.0 | 0.0 | 35.0 | 37.0 | — | — | — |
| Exploration & Production | 108.9 | 144.2 | 177.8 | 180.7 | 183.4 | 128.0 | 65.0 | 0.0 |
| Corporate & Other | (41.8) | (21.5) | (54.6) | (22.3) | (31.0) | 7.0 | 3.0 | (70.0) |
| Total Core EBIT | 757.4 | 898.6 | 871.7 | 1,009.7 | 1,284.4 | 1,740.0 | 2,054.0 | 2,224.6 |
| Energy Services | 28.0 | (22.9) | — | — | (107.0) | (119.0) | (68.0) | 75.0 |
| **EBIT (before Min. Interest)** | **785.4** | **875.7** | **871.7** | **1,009.7** | **1,177.4** | **1,621.0** | **1,986.0** | **2,299.6** |
| Net Interest Expense | (300.0) | (273.5) | (283.3) | (273.6) | (401.0) | (550.0) | (656.0) | (700.0) |
| Dividends on Pfd. Stock of Sub. Co. | (2.1) | (19.9) | (32.5) | (34.0) | (69.0) | (77.0) | (76.0) | (76.0) |
| Minority Interest | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Enron Oil & Gas | 0.0 | 0.0 | 0.0 | (57.0) | (34.0) | (24.0) | 6.0 | 0.0 |
| Other Minority Interest | 0.0 | 0.0 | 0.0 | (10.0) | (10.0) | (53.0) | (141.0) | (145.6) |
| Total Minority Interest | (27.6) | (23.5) | (17.0) | (66.7) | (80.0) | (77.0) | (135.0) | (145.6) |
| **EBIT** | **455.7** | **558.8** | **538.8** | **635.3** | **627.5** | **917.0** | **1,119.0** | **1,378.0** |
| Current | (79.2) | (50.2) | 14.4 | 33.2 | (286.0) | (132.0) | (144.6) | (162.3) |
| Deferred | (51.2) | (93.0) | (128.6) | (207.0) | 174.0 | (87.0) | (12.0) | (40.0) |
| Total Income Taxes | (130.4) | (143.1) | (114.2) | (173.8) | (112.0) | (219.0) | (156.6) | (202.3) |
| Tax Rate | 28.6% | 25.6% | 21.2% | 27.4% | 17.8% | 23.9% | 14.0% | 14.7% |
| Recurring Net Income | 325.2 | 415.7 | 424.6 | 461.5 | 515.5 | 698.0 | 962.4 | 1,175.7 |
| Total Preferred Dividends | (16.8) | (15.8) | (15.2) | (15.6) | (17.0) | (17.0) | (66.0) | (76.0) |
| **Recurring Net to Common** | **308.4** | **399.9** | **409.4** | **445.9** | **498.5** | **681.0** | **904.4** | **1,099.7** |
| Nonrecurring / Special Items | 62.8 | 37.6 | 96.4 | 120.2 | (413.0) | 5.0 | (200.6) | 0.0 |
| Other Nonrecurring | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Extraordinary | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net Income to Common | 371.2 | 437.5 | 505.9 | 566.2 | 85.5 | 686.0 | 703.8 | 1,099.7 |
| **Basic EPS:** | | | | | | | | |
| Recurring Earnings | $0.65 | $0.82 | $0.84 | $0.91 | $0.92 | $1.06 | $1.29 | $1.55 |
| Reported Basic Earnings | $0.78 | $0.90 | $1.04 | $1.15 | $0.16 | $1.07 | $1.01 | $1.55 |
| **Diluted EPS:** | | | | | | | | |
| **Recurring Earnings** | **$0.61** | **$0.78** | **$0.79** | **$0.85** | **$0.87** | **$1.00** | **$1.18** | **$1.37** |
| Nonrecurring / Special Items | $0.12 | $0.07 | $0.18 | $0.22 | ($0.70) | $0.01 | ($0.26) | $0.00 |
| Other Nonrecurring | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 |
| Extraordinary | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 | $0.00 |
| Reported Diluted Earnings | $0.73 | $0.85 | $0.97 | $1.08 | $0.17 | $1.01 | $1.00 | $1.47 |
| Primary Shares Outstanding | 478.0 | 486.9 | 487.1 | 492.1 | 544.3 | 642.2 | 698.9 | 708.0 |
| Diluted Shares Outstanding | 530.6 | 533.1 | 534.9 | 540.4 | 591.4 | 695.1 | 768.8 | 800.0 |
| Dividends Per Share | $0.36 | $0.38 | $0.41 | $0.43 | $0.46 | $0.48 | $0.50 | $0.53 |
| Book Value | $5.18 | $5.63 | $6.22 | $7.29 | $10.08 | $10.66 | $11.17 | $12.19 |
| Avg Return On Equity | 11.8% | 13.9% | 12.8% | 11.7% | 8.7% | 9.4% | 10.5% | 11.3% |
| Return on Total Capital | 9.4% | 9.5% | 9.0% | 8.3% | 9.0% | 12.3% | 7.5% | 7.8% |

Source: Company information and Prudential Securities estimates.

## *Figure 5. Enron Corp. Cash Flow Statement*

| (Dollars in millions, except per-share data) | 1998 | | | | | 1999 | | | | | 2000E |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1Q | 2Q | 3Q | 4Q | Year | 1Q | 2Q | 3Q | 4Q | Year | Year |
| **Sources of Cash:** | | | | | | | | | | | |
| Net Income | $210.0 | $140.0 | $164.0 | $172.0 | $686.0 | $118.0 | $203.0 | $141.0 | $241.8 | $703.8 | $1,099.7 |
| DD&A | 182.0 | 190.0 | 215.0 | 240.0 | 827.0 | 215.0 | 236.0 | 225.0 | 232.0 | 908.0 | 914.0 |
| Deferred Income Taxes | 54.0 | 6.0 | 49.0 | (22.0) | 87.0 | 2.0 | (13.0) | (27.0) | 50.0 | 12.0 | 40.0 |
| Amort of Def'd Contract | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 3.0 | 2.0 | 2.0 | 2.0 | 9.0 | 9.0 |
| Other (incl non-cash charges) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 131.0 | 0.0 | 0.0 | 0.0 | 131.0 | 0.0 |
| Exploration & Lease Exp. | 34.0 | 26.0 | 34.0 | 24.0 | 118.0 | 25.0 | 20.0 | 10.0 | 26.0 | 81.0 | 104.0 |
| Cash Flow From Ops(CFO) | $480.0 | $362.0 | $462.0 | $414.0 | $1,718.0 | $494.0 | $448.0 | $351.0 | $551.8 | $1,844.8 | $2,166.7 |
| **Per Share:** | | | | | | | | | | | |
| **Cash Flow** | **$0.79** | **$0.57** | **$0.70** | **$0.63** | **$2.68** | **$0.75** | **$0.63** | **$0.49** | **$0.77** | **$2.64** | **$3.06** |
| **EBITDA** | **$1.07** | **$0.84** | **$0.94** | **$0.97** | **$3.81** | **$1.14** | **$1.00** | **$1.03** | **$0.99** | **$4.14** | **$4.54** |
| CF/Share Growth % | | | | | 28% | | | | | -1% | 16% |
| Changes In Working Capital | (158.0) | (502.0) | 288.0 | 139.0 | (233.0) | (556.0) | (353.0) | (163.0) | 0.0 | (1,072.0) | 0.0 |
| Total Sources of Cash | 322.0 | (140.0) | 750.0 | 553.0 | 1,485.0 | (62.0) | 95.0 | 188.0 | 551.8 | 772.8 | 2,166.7 |
| **Uses of Cash:** | | | | | | | | | | | |
| Capital Expenditures | 288.0 | 297.0 | 646.0 | 674.0 | 1,905.0 | 519.0 | 450.0 | 1,053.0 | 275.0 | 2,297.0 | 1,100.0 |
| Common Dividends | 72.4 | 75.8 | 78.1 | 82.5 | 309.0 | 82.0 | 88.3 | 89.0 | 93.6 | 353.0 | 375.4 |
| Free Cash Flow | ($38.4) | ($512.8) | $25.8 | ($203.5) | ($728.9) | ($663.0) | ($443.3) | ($954.0) | $183.2 | ($1,877.2) | $691.3 |
| CFFO | $480.0 | $362.0 | $462.0 | $414.0 | $1,718.0 | $494.0 | $448.0 | $351.0 | $551.8 | $1,844.8 | $2,166.7 |
| Gains on assets sales investments | (27.0) | (5.0) | 1.0 | (51.0) | (82.0) | (40.0) | (25.0) | (396.0) | 0.0 | (461.0) | 0.0 |
| Changes in working capital | (158.0) | (502.0) | 288.0 | 139.0 | (233.0) | (556.0) | (353.0) | (163.0) | 482.0 | (590.0) | (300.0) |
| Net assets from price RM activities | (249.0) | (4.0) | (205.0) | 808.0 | 350.0 | (518.0) | 765.0 | (192.0) | 0.0 | 55.0 | 0.0 |
| Amoritiz. of prod. payment transaction | (11.0) | (10.0) | (11.0) | 117.0 | 85.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other | 117.0 | (124.0) | (87.0) | (104.0) | (198.0) | (40.0) | (213.0) | 395.0 | 0.0 | 142.0 | 0.0 |
| **Net Operating Cash Flow** | **152.0** | **(283.0)** | **448.0** | **1,323.0** | **1,640.0** | **(660.0)** | **622.0** | **(5.0)** | **1,033.8** | **990.8** | **1,866.7** |
| Investing Activities: | | | | | | | | | | | |
| Capital expenditures | (288.0) | (297.0) | (646.0) | (674.0) | (1,905.0) | (519.0) | (450.0) | (1,053.0) | (275.0) | (2,297.0) | (1,100.0) |
| Proceeds from sale of assets | 3.0 | 55.0 | 1.0 | 180.0 | 239.0 | 43.0 | 95.0 | 107.0 | 0.0 | 245.0 | 0.0 |
| Equity investments | (59.0) | (107.0) | (1,332.0) | (161.0) | (1,659.0) | (409.0) | (239.0) | (70.0) | 0.0 | (718.0) | 0.0 |
| Acquisition of subsidiary stock | — | (180.0) | — | — | (180.0) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Business acquisitions, net | 0.0 | (25.0) | (62.0) | (17.0) | (104.0) | (38.0) | (2.0) | (173.0) | 0.0 | (213.0) | 0.0 |
| Other | (250.0) | (109.0) | (221.0) | 224.0 | (356.0) | (207.0) | (133.0) | (107.0) | 0.0 | (447.0) | 0.0 |
| **Net Investing Cash Flow** | **(594.0)** | **(663.0)** | **(2,260.0)** | **(448.0)** | **(3,965.0)** | **(1,130.0)** | **(729.0)** | **(1,296.0)** | **(275.0)** | **(3,430.0)** | **(1,100.0)** |
| Financing Activities: | | | | | | | | | | | |
| Net change in short-term borrowings | 623.0 | 146.0 | 1,228.0 | (2,155.0) | (158.0) | 1,119.0 | 182.0 | 737.0 | 0.0 | 2,038.0 | 0.0 |
| Long-term debt | (42.0) | 6.0 | 901.0 | 168.0 | 1,033.0 | 46.0 | (563.0) | 670.0 | 0.0 | 153.0 | 0.0 |
| Preferred subsidiary securities | 0.0 | 0.0 | 0.0 | 8.0 | 8.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Common stock | 2.0 | 842.0 | 23.0 | 0.0 | 867.0 | 839.0 | 50.0 | 0.0 | 0.0 | 889.0 | 0.0 |
| Subsidiary equity | — | — | — | 828.0 | 828.0 | 0.0 | 513.0 | 0.0 | 0.0 | 513.0 | 0.0 |
| Dividends paid | (99.0) | (105.0) | (103.0) | (107.0) | (414.0) | (113.0) | (114.0) | (119.0) | (102.0) | (448.0) | (424.2) |
| Net change in treasury stock | 3.0 | 4.0 | (1.0) | 7.0 | 13.0 | 119.0 | 62.0 | 42.0 | (201.0) | 22.0 | 0.0 |
| Other | (42.0) | 55.0 | (28.0) | 104.0 | 89.0 | (35.0) | (33.0) | 1.0 | 0.0 | 0.0 | (300.0) |
| **Net Financing Cash Flow** | **445.0** | **948.0** | **2,020.0** | **(1,147.0)** | **2,266.0** | **1,975.0** | **97.0** | **1,331.0** | **(303.0)** | **3,100.0** | **(724.2)** |
| **Beginning Cash** | **170.0** | **173.0** | **175.0** | **383.0** | **170.0** | **111.0** | **296.0** | **286.0** | **316.0** | **111.0** | **771.8** |
| Change in Cash | 3.0 | 2.0 | 208.0 | (272.0) | (59.0) | 185.0 | (10.0) | 30.0 | 455.8 | 660.8 | 42.5 |
| **Ending Cash** | **$173.0** | **$175.0** | **$383.0** | **$111.0** | **$111.0** | **$296.0** | **$286.0** | **$316.0** | **$771.8** | **$771.8** | **$814.3** |

Source: Company information and Prudential Securities estimates.

## *Figure 6. Integrated Natural Gas Company Universe—Valuation Screen*

| | Rating | Risk | Stock Price 01/21/00 | Target Price | Potential Apprec. | EPS From Cont. Ops. 1998 | EPS From Cont. Ops. 1999E | EPS From Cont. Ops. 2000E | P/E Ratio 1999E | P/E Ratio 2000E | CF/Share 1998 | CF/Share 1999E | CF/Share 2000E | CF Ratio 1999E | CF Ratio 2000E |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Integrated Pipelines** | | | | | | | | | | | | | | | |
| Coastal Corp. (CGP) (4) | SB | Low | $37.25 | $44 | 18.1% | $2.03 | $2.31 | $2.75 | 16.1 | 13.5 | $4.47 | $4.91 | $5.31 | 7.6 | 7.0 |
| Columbia Energy (CG) (2) | Hold | Low | 65.69 | 64 | -2.6% | 3.07 | 3.40 | 4.00 | 19.3 | 16.4 | 5.68 | 7.01 | 7.10 | 9.4 | 9.3 |
| Consol. Natural Gas (CNG) | Hold | Low | 68.06 | 68 | -0.1% | 2.93 | 3.14 | 3.75 | 21.7 | 18.2 | 6.80 | 6.57 | 7.89 | 10.4 | 8.6 |
| El Paso Energy (EPG)! (2) | SB! | Low | 33.88 | 50 | 47.6% | 1.53 | 1.52 | 2.45 | 22.3 | 13.8 | 6.24 | 6.81 | 8.15 | 5.0 | 4.2 |
| Enron Corp. (ENE) (4) | SB | Mod. | 71.63 | 85 | 18.7% | 1.00 | 1.18A | 1.37 | 60.7 | 52.3 | 2.68 | 2.64A | 3.06 | 27.1 | 23.4 |
| Equitable Reso. (EQT) (4) | SB | Low | 36.25 | 50 | 37.9% | 0.69 | 2.09 | 2.65 | 17.3 | 13.7 | 2.27 | 5.49 | 6.78 | 6.6 | 5.3 |
| Kinder Morgan Inc. (KMI) | Hold | Mod. | 29.50 | 25 * | -15.3% | 1.00 | 0.13 | 1.08 | NM | 27.3 | 2.84 | 0.32 | 1.97 | 92.2 | 15.0 |
| Midcoast Energy (MRS) (4) | SB | Mod. | 17.00 | 23 | 36.5% | 1.25 | 1.55 | 1.83 | 11.0 | 9.3 | 1.85 | 2.33 | 3.51 | 7.3 | 4.8 |
| Questar Corp. (STR) | Hold | Low | 16.25 | 18 | 10.8% | 1.10 | 1.21 | 1.31 | 13.4 | 12.4 | 2.49 | 3.21 | 3.15 | 5.1 | 5.2 |
| Williams Cos. (WMB) | Accum. | Low | 39.19 | 36 * | -8.1% | 0.73 | 0.45 | 0.52 | 87.1 | 75.4 | 2.54 | 3.14 | 2.71 | 12.5 | 14.5 |
| Simple Average | | | | | | | | | 29.9 | 25.2 | | | | 18.3 | 9.7 |
| **Unregulated Energy Cos.** | | | | | | | | | | | | | | | |
| Dynegy Inc. (DYN) (1) (2) | Accum. | Mod. | $30.19 | $26 * | -13.9% | $0.59 | $0.85 | $2.22 | 35.5 | 13.6 | $1.47 | $1.86 | $2.01 | 16.2 | 15.0 |
| Independent Energy (INDYY) (4) (5) | SB | High | 46.50 | 42 * | -9.7% | (0.03) | 0.22A | 0.84 | NM | 55.4 | 0.04 | 0.32A | 2.33 | NM | 20.0 |
| Western Gas Reso. (WGR) | Accum. | High | 13.38 | 18 | 34.6% | (0.65) | (0.20) | 0.11 | NM | NM | 1.77 | 1.61 | 2.39 | 8.3 | 5.6 |
| Simple Average | | | | | | | | | 35.5 | 34.5 | | | | 8.2 | 13.5 |
| ***Yield-Oriented Securities*** | | | | | | | | | | | | | | | |
| **Integrated Utilities** | | | | | | | | | | | | | | | |
| Duke Energy (DUK) (4) | Hold | Low | $56.50 | $59 | 4.4% | $3.28 | $3.65A | $4.00 | 15.5 | 14.1 | $6.02 | $8.18A | $7.28 | 6.9 | 7.8 |
| PG&E Corp. (PCG) (4) | Hold | Mod. | 22.44 | 21 * | -6.4% | 1.94 | 1.72 | 1.70 | 13.0 | 13.2 | 7.69 | 7.45 | 7.62 | 3.0 | 2.9 |
| USEC Inc. (USU) (3) (4) | Hold | High | 6.50 | 8 | 23.1% | 0.97 | 1.21 | 1.20 | 5.4 | 5.4 | 1.52 | 1.72 | 2.55 | 3.8 | 2.5 |
| Simple Average | | | | | | | | | 11.3 | 10.9 | | | | 4.6 | 4.4 |
| **Master Limited Partnerships** | | | | | | | | | | | | | | | |
| Enterprise Products Ptrs. (EPD) (4) | Accum. | Low | $19.38 | $25 | 29.0% | 0.56 | 1.51 | 1.61 | 12.8 | 12.0 | ($0.30) | $1.46 | $1.89 | 13.3 | 10.3 |
| Kinder Morgan Energy (KMP) (4) | SB | Low | 44.00 | 52 | 18.2% | 2.09 | 2.38 | 2.58 | 18.5 | 17.1 | 2.79 | 3.11 | 3.57 | 14.1 | 12.3 |
| Star Gas Partners (SGU) (4) | Hold | Mod. | 14.38 | 18 | 25.2% | (0.27) | 0.08 | 0.53 | NM | 27.1 | 2.50 | 4.13 | 2.68 | 3.5 | 5.4 |
| Simple Average | | | | | | | | | 15.7 | 18.7 | | | | 10.3 | 9.3 |
| Total Group Performance | | | $667.94 | | | | | | | | | | | | |
| Dow Jones Industrials | | | 11,497.10 | | | | | | | | | | | | |
| S&P 400 | | | 1834.74 | | | $38.37 | $49.86 | $52.58 | 36.8 | 34.9 | | | | | |
| S&P 500 | | | 1469.20 | | | $37.71 | $45.94 | $49.50 | 32.0 | 29.7 | | | | | |

SB= Strong Buy; Accum.= Accumulate; Mod.= Moderate; != Single Best Idea; * Under Review

Notes: 1) Indicates fiscal 2000 earnings estimates are pro forma, pending closing of merger.
2) Price targets based on expected merger.
3) Fiscal year ends 6/30 for USEC Inc. and Independent Energy and 9/30 for Star Gas.
4) Prudential Securities Incorporated and/or its affiliates and its subsidiaries have managed or comanaged a public offering of securities for this company.
5) Prudential Securities Incorporated makes a primary over-the-counter market in the shares of this company.

Source: Company information; Prudential Securities estimates.

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