Industry: Natural Gas
February 3, 1997
GT0224

Steven A. Parla, C.F.A. 212/325-3145 *sparla@csfbg.csfb.com*
Vince Salvato 212/325-2518 *vsalvato@csfbg.csfb.com*

BUY

Enron Corp. (ENE)

Summary

Maintaining our Buy on ENE despite its slower 1997 EPS outlook as it is the best positioned company to capitalize on further growth in wholesale gas marketing, wholesale electric marketing, and retail gas and electric marketing.

Large Cap

Price 1/31/97[1]	Target (12 Months)	Dividend	Yield	Mkt. Value (Millions)	52-Week Price Range
41 1/4	$50	$0.90	2.2%	$10,494	35–48

	Annual EPS	Prev. EPS	Abs. P/E	Rel. P/E	EBITDA/ Share
12/97E	$2.60		15.9X	87%	$7.15
12/96A	2.31		17.9	89	6.40
12/95A	2.07		19.9	95	5.82

	March	June	September	December	FY End
1996A	$0.62	$0.45[2]	$0.48	$0.52	Dec. 31
1995A	0.72	0.34	0.39	0.62	

ROIC (12/95)	—	**Total Debt (9/96)**	$3.6 bil.	**Book Value/Share (12/95)**	$13.58
WACC (12/95)	—	**Debt/Total Capital (12/95)**	37%	**Common Shares**	254.4 mil.
EVA® (Trend)	Up	**Est. 5-Yr. EPS Growth**	15%	**Est. 5-Yr. Div. Growth**	5%

[1]On 1/31/97 DJIA closed at 6813 and S&P 500 at 786.2.

[2]Adjusted for $18.2 million gain on sale of EOG stock and $16.1 million aftertax litigation reserve.

➡ **Enron is one of the world's largest integrated energy providers with operations in energy marketing, international development, oil & gas E&P, electricity, and natural gas transmission and storage.**

Viewpoint

Enron Corp. held a two-day analyst seminar on January 23-24, 1997. Management reiterated its statement that 1997 EPS growth is likely to be in the "lower half" of Enron's expected 10-15% annual EPS growth goal. Investors will recall that in mid 1996, management stated after years of 15% annual EPS growth, it now expects growth of 10-15% in any single year—but on a compound basis it still expects 15% growth through the year 2000. Thus, after EPS growth of 11.6% in 1996 to $2.31 from $2.07 in 1995, most Street estimates have been reduced to the $2.60 range from $2.70 for 1997, implying EPS growth of about 12.5% this year.

In our opinion, reasons for the current EPS growth slowdown include, but are not necessarily limited to:

- While retail gas and electric marketing could be "equal to or bigger than" all of Enron today in five to seven years, according to chairman and CEO Ken Lay, building a retail gas and electric presence will be expensive and time-consuming. Large expenditures for a retail marketing infrastructure and advertising will negatively affect earnings in 1997 and 1998.

- The exact timing of the realization of international earnings remains lumpy and subject to many political, regulatory, and other forces beyond Enron's control. In addition, the company noted that increased competition for international projects has reduced returns about 300-400 basis points.

- We maintain our view that wholesale electric marketing will be huge and Enron will be dominant. However, the vested interests of incumbent, fully-integrated electric utilities will continue to prevent a rapid, optimal opening of full wholesale electric marketing.

- Wholesale gas marketing has matured. Despite having additional growth and improved profitability as consolidation among gas marketers continues, the blistering growth rate of the past few years has clearly slowed.

- The continued selldown of businesses and partial business lines (i.e., Enron Oil & Gas) has been very positive overall for Enron, but leaves less residual earnings and earnings growth.

As noted by management since mid 1996 and discussed by us earlier, earnings growth at Enron has clearly slowed in 1996-1997. This has been well noted by the market and (we believe) reflected in the contraction in Enron's multiple to 16 times estimated 1997 EPS, about in line with the gas pipeline group—a group itself experiencing impressive earnings growth in the past few years of optimal and perhaps better-than-normal industry conditions.

We maintain our Buy on Enron despite the 1997 EPS growth outlook for one major reason: *It is absolutely the best-positioned company to capitalize on further growth in wholesale gas marketing, wholesale electric marketing, and retail gas and electric marketing*, business lines that we continue to believe hold huge profit potential. We acknowledge that near-term EPS growth has slowed and this appears to be reflected in the multiple. This could result in Enron common being only a market performer in 1997 as we await the acquisition of Portland General and further development of wholesale electric and retail gas and electric markets.

Highlights from the January Meeting

Enron Capital & Trade

ECT for the first time outlined a retail gas and electric marketing plan and long-term profitability goals. Given the huge number of legislative, regulatory, competitive, and market-size vagaries associated with the deregulation of wholesale electric and retail gas and electric markets, these should obviously be used as guidance.

ECT's vision of 2001 includes 26 states with full or partial retail gas and electric access. ECT will spend $75 million on average over the next three years to build an initial marketing infrastructure of 9,000 employees in 95 regional branches. ECT's eight million retail customers will generate *gross revenue* of $20 billion. ECT hopes to achieve a 1-2% return on gross sales, or $200-400 million of EBIT, by providing retail gas all-in at 10-15% less in the Northeast and other high-cost gas regions and electricity at almost 10% below competitors in high-cost electric markets such as California.

Enron Capital & Trade continues to increase its market share and profitability in gas marketing and strengthen its position as the leading electricity wholesaler. This industry position, together with colder weather and tight and volatile natural gas commodity markets, drove 1996 EBIT to $280 million versus $232 million despite a net $42 million increase in ECT's reserves for "credit" and "prudency."

ECT noted a margin improvement above and beyond current "gas heaven" industry conditions as natural gas wholesaling consolidates. According to ECT data, the top ten gas marketers have almost a 90% market share today versus 48% in 1990. ECT also noted that the top ten electric wholesalers already have almost 75% of today's small but rapidly growing wholesale electric market. Those data imply that a substantial reduction in margins may be far less likely in the early years of electric marketing, unlike the gas experience.

Enron International

Enron International again defined the huge worldwide market for energy infrastructure projects, but conceded that increased competition has reduced returns by 300-400 basis points. The company stressed its multiple capabilities across a spectrum of skills, and its integrated strategies to increase its chance of success as well as profitability, while minimizing risk. The company has a $20 billion portfolio of projects in various stages of development. International has an aggressive goal of closing seven new development projects in 1997.

Gas Pipeline Group

Despite faster growth in other areas, the Gas Pipeline group still contributed 40% of Enron's 1996 EBIT. The group continues to enhance customer services, reduce O&M and other operating costs, and produce EBIT growth generally better than anticipated (5% annually). Included in future expansion plans is an $800 million expansion of the Northern Border Pipeline that will increase Canadian imports by 700 MMcf/day when completed in November 1998, as well as smaller expansions of Northern Natural and Transwestern.

Enron Oil & Gas

Enron Oil & Gas, 53% owned by Enron Corp., continues with its now well-known strategies to increase production 10% annually, drive down costs, and maximize its marketing and other nonproduction revenue. Year-end 1996 reserves were 4 Bcf equivalent, 88% natural gas. Excluding its deep Wyoming reserves, EOG has 2.8 Bcf equivalent in total reserves. The company expects tight U.S. gas markets "through 1998" but may look to increase commodity price hedges for 1998 and beyond. However, the company does not expect to hedge to past levels as a percentage of total production.

Portland General Merger

A presentation on the pending Portland General acquisition stressed its low-cost generation and interconnects to 32 other service territories (see our July 29, 1996 report on the ENE/PGN merger proposal for detail). Enron still wants to close the merger in "mid 1997" after an expected March 17 Oregon PUC decision. However, the company acknowledged the risks within numerous issues raised by the PUC staff, noting that many of the staff's positions are "onerous." Our concern regarding the timely and satisfactory closing of the PGN merger, once almost nonexistent, has increased. While we had considered the closing a complete certainty, our current concern relates to the PUC staff's conditions for the proposed merger.

N.B.: CREDIT SUISSE FIRST BOSTON CORPORATION may have, within the last three years, served as a manager or co-manager of a public offering of securities for or makes a primary market in issues of any or all of the companies mentioned. Closing prices are as of January 31, 1997':

Enron Oil & Gas (EOG, 23 1/4, Hold)
Portland General (PGN, 39 1/4)

Table 1
Natural Gas Companies: Earnings Estimates and Comparable Multiples

		Shares	Market	Earnings Per Share			P/E Ratio			Book Value		Cash Flow Data			Dividend		
	Price	Outstanding	Cap							Latest	Market	1996E	Price/	Ent. Val.	Annual	Current	
Company	1/31/97	(Thousands)	(Thousands)	1995A	1996E	1997E	1995A	1996E	1997E	Per Share	to Book	Per Share	Cash Fl.	/EBITDA	Rate	Yield	Symbol
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
Gas Pipelines																	
Coastal Corp.	$48.375	105,564	$5,106,659	$2.30	$2.88 A	$3.25	21.0 x	16.8 x	14.9 x	$26.44	1.83 x	$7.15	6.77 x	8.15 x	$0.40	0.8 %	CGP
El Paso Natural (b)	53.875	55,755	3,003,801	2.47	2.85 A	3.19	21.8	18.9	16.9	31.57	1.71	5.79	NM	NM	1.46	2.7	EPG
Enron Corp. (BUY)	41.250	253,684	10,464,465	2.07	2.31 A	2.60	19.9	17.9	15.9	13.47	3.06	5.15	8.01	9.11	0.90	2.2	ENE
Sonat Inc. (BUY)	53.250	86,251	4,592,866	1.31	2.33 A	2.60	40.6	22.9	20.5	17.58	3.03	6.34	8.40	8.48	1.08	2.0	SNT
TransCan PipeLn (c)	24.100	205,800	4,959,780	1.75	1.85 A	1.90	13.8	13.0	12.7	14.29	1.69	3.95	6.10	7.02	1.08	4.5	TRP
Williams Companies	40.000	168,231	6,729,240	1.68	2.10 A	2.35	23.8	19.0	17.0	18.88	2.12	5.03	7.95	9.12	1.04	2.6	WMB
							----	----	----		----		----	----		---	
Gas Pipeline Averages							23.5 x	18.1 x	16.3 x		2.24 x		7.45	8.38 x		2.5 %	
Integrated Cos.																	
Columbia Gas System	$65.125	55,200	$3,594,900	$3.04	$4.68 A	$4.80	21.4 x	13.9 x	13.6 x	$27.17	2.40 x	$10.00	6.51 x	7.28 x	$0.60	0.9 %	CG
Consol. Natural (BUY)	55.625	94,183	5,238,929	2.29	3.25	3.35	24.3	17.1	16.6	23.21	2.40	6.45	8.62	7.62	1.94	3.5	CNG
Equitable Resources	32.500	35,130	1,141,725	1.23	1.55	1.95	26.4	21.0	16.7	20.99	1.55	4.05	8.02	7.24	1.18	3.6	EQT
Questar Corp.	39.125	40,842	1,597,943	2.00	2.25	2.50	19.6	17.4	15.7	18.38	2.13	5.10	7.67	7.05	1.22	3.1	STR
							----	----	----		----		----	----		----	
Integrated Co. Averages							22.9 x	17.3 x	15.6 x		2.12 x		7.71 x	7.30 x		2.8 %	
Gas Distributors																	
Atlanta Gas Light	$20.875	55,527	$1,159,126	$1.33	$1.37 A	$1.45	15.7 x	15.2 x	14.4 x	$10.84	1.93 x	$3.06	6.82 x	8.20 x	$1.08	5.2 %	ATG
Brooklyn Union Gas	29.625	49,773	1,474,525	1.90	1.96 A	2.10	15.6	15.1	14.1	18.30	1.62	3.70	8.01	7.86	1.46	4.9	BU
MCN Corp.	32.375	67,028	2,170,032	1.48	1.68 A	1.80	21.9	19.3	18.0	11.29	2.87	4.05	7.99	9.72	0.97	3.0	MCN
NICOR Inc.	36.125	50,073	1,808,887	1.96	2.42 A	2.40	18.4	14.9	15.1	14.69	2.46	4.90	7.37	6.65	1.32	3.7	GAS
Washington Gas Light	22.125	43,573	964,053	1.41	1.94 A	1.70	15.7	11.4	13.0	13.46	1.64	3.40	6.51	6.18	1.14	5.2	WGL
							----	----	----		----		----	----		----	
Gas Distributor Averages							17.5 x	15.2 x	14.9 x		2.10 x		7.34 x	7.72 x		4.4 %	
S&P 500	786.160	----	----	38.72	40.49	42.93	20.3 x	19.4 x	18.3 x	225.00	3.49 x	75.00	10.48 x		$14.75	1.9 %	SPX

(a) Based on continuing operations; excludes significant non-recurring items.
(b) We have not yet initiated coverage. Estimates are First Call consensus.
(c) Canadian dollars.

E - Credit Suisse First Boston Estimate; A - Actual; R - Restricted
NM - Not meaningful; data are excluded from calculations
Note - Book value as of June 30, 1996. All companies rated Hold unless otherwise indicated.

Table 2
Earnings Model, 1993–19997E
$ in millions, except per share data

			1995A					1996A					
	1993	1994	1st QA	2nd QA	3rd QA	4th QA	Year	1st QA	2nd QA	3rd QA	4th QA	Year	1997E
Operating income													
ENE Operations	382.2	403.1	154.0	69.1	82.7	109.7	415.5	142.5	101.4	97.5	139.0	480.4	500.0
ENE Capital & Trade	168.8	225.1	51.4	46.7	60.4	74.0	232.5	97.7	52.1	73.8	56.0	279.6	330.0
Domestic Processing	28.0	(22.9)	--	--	--	--	--	--	--	--	--	--	--
International	131.3	147.7	51.2	24.3	39.8	26.8	142.1	40.3	39.3	37.3	35.0	151.9	180.0
Explorat & Production	108.9	162.4	58.3	84.5	52.9	45.0	240.7	29.7	76.9	49.6	43.0	199.2	250.0
Other	(35.0)	14.1	25.7	(7.9)	(1.5)	(70.9)	(54.6)	10.0	(11.8)	(0.7)	19.0	16.5	40.0
	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----	-----
Total	784.2	929.5	340.6	216.7	234.3	184.6	976.2	320.2	257.9	257.5	292.0	1,127.6	1,300.0
Interest expense, net	300.0	274.9	67.0	70.9	76.8	69.5	284.2	69.7	65.4	65.2	74.0	274.3	275.0
Subsid Preferred Div		19.9	7.8	7.9	7.9	8.3	31.9	7.8	8.1	8.1	10.0	34.0	35.0
Minority Interest	27.6	29.5	5.9	9.7	6.5	5.2	27.3	10.3	19.2	12.9	15.0	57.4	56.0
Pretax income	456.6	605.2	259.9	128.2	143.1	101.6	632.8	232.4	165.2	171.3	193.0	761.9	934.0
Income taxes	84.8	165.5	82.4	40.7	43.6	(28.6)	138.1	78.2	50.6	48.4	61.0	238.2	280.2
	18.6%	27.3%	31.7%	31.8%	30.5%	-28.1%	21.8%	33.6%	30.6%	28.3%	31.6%	31.3%	30.0%
Net income	371.8	439.7	177.5	87.5	99.5	130.2	494.6	154.2	114.6	122.9	132.0	523.7	653.8
Preferred dividends	16.9	15.2	3.7	3.8	3.9	4.0	15.4	3.9	3.9	4.0	4.0	15.8	15.0
Net to common	354.9	424.5	173.8	83.7	95.6	126.2	479.2	150.3	110.7	118.9	128.0	507.9	638.8
Average shares	239.0	243.5	242.5	244.0	243.9	243.6	243.5	244.2	246.3	246.8	247.0	246.1	246.0
EPS	$1.48	$1.74	$0.72	$0.34	$0.39	$0.52	$1.97	$0.62	$0.45	$0.48	$0.52	$2.06	$2.60
Fully Diluted	$1.40	$1.65	0.65	0.31	0.36	0.47	$1.78	0.56	0.41	0.44	0.47	1.87	$2.39
Nonrecurring items	($0.16)	$0.06	$0.07	$0.03	$0.00	$0.00	$0.10	$0.24	$0.01			$0.25	
Reported EPS	$1.32	$1.80	$0.79	$0.37	$0.39	$0.52	$2.07	$0.86	$0.46	$0.48	$0.52	$2.31	$2.60

1995-1Q gain on sale of gathering/processing assets, $26.9 pre, $17.5 after.2Q gain on sale of $10 pre, $6.5 after tax on sale of gathering and processing facilities
3Q gain on sale of gathering/processing assets, $9.2pre, $6.0 after; Charge by EOTT for West Coast processing termination, $8.5 pre, $5.5 after tax.
4Q $83.4 million charge for ENE Operations litigation/regulatory reserve, $75 million pretax charge at ECT for "Clean Fuel Costs", basically as asset write-down.
4Q Sale of 20% interest in EOG, resulting in $293 pre-tax gain, $161 after tax gain on sale.
1996-1Q gain on sale of 2Q gain on sale of EOG shares, $28.0 million pre-tax, $18.2 million after-tax; Lititagation reserve, $24.7 pre-tax, $16.1 million after-tax.
4Q $18 pre, $12 after-tax litigation gain; $122 pre, $61 after-tax EOG stock sale gain; $83 pre, $54 after-tax litigation reserve.

	1993	1994	1995A Year	1996A Year	1997E
Net to common	354.9	424.5	479.2	507.9	638.8
Depreciation	458.2	441.3	500.0	537.5	550.0
Deferred taxes	51.2	93.0	45.0	50.0	60.0
Lease impair & explo exp.	75.7	84.0	90.0	100.0	100.0
Total	940.0	1,042.8	1,114.2	1,195.4	1,348.8
Cash flow per share	$3.93	$4.28	$4.58	$4.86	$5.48
Fully Diluted	$3.81	$4.15	$4.43	$4.70	$5.29
Common dividends	170.7	188.7	243.9	244.8	257.0
Capital expenditures	695.0	661.0	900.0	1,700.0	1,700.0
EBITDA	$1,215	$1,321	$1,417	$1,574	$1,759
Internal cash flow rate	110.7%	129.2%	96.7%	55.9%	64.2%

CREDIT SUISSE | FIRST BOSTON

Americas

Eleven Madison Avenue
New York, NY 10010, U.S.A.
1 212 325 2000

Atlanta	1 404 656 9500	Mexico City	525 202 6000
Boston	1 617 556 5500	Philadelphia	1 215 851 1000
Buenos Aires	1 541 394 3100	Portland	1 207 780 6210
Chicago	1 312 750 3000	San Francisco	1 415 765 7000
Houston	1 713 220 6700	São Paulo	55 11 822 4862
Los Angeles	1 213 253 2000	Toronto	1 416 947 2600

Europe

One Cabot Square
London E14 4QJ, England
44 171 888 8888

Amsterdam	31 20 575 4444	Paris	33 1 40 76 8888
Budapest	36 1 202 2188	Prague	42 2 248 10937
Frankfurt	49 69 7534 0	Vienna	43 1 512 3023
Geneva	41 22 707 0130	Warsaw	48 22 695 0050
Madrid	34 1 532 0303	Zug	41 41 726 1020
Milan	39 2 7702 1	Zurich	41 1 335 7220
Moscow	7 501 967 8200		

Pacific

Shiroyama Hills
4-3-1 Toranomon
Minato-ku, Tokyo 105, Japan
81 3 5404 9000

Auckland	64 9 302 5500	Seoul	82 2 399 7355
Beijing	86 10 501 4508	Singapore	65 226 5088
Hong Kong	852 2847 0388	Sydney	61 2 394 4400
Melbourne	61 3 9 280 1666	Wellington	64 4 474 4400
Osaka	81 6 243 0789		