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PRESENTATION

Operator

Good day, and welcome to the ALLETE Fourth Quarter 2018 Financial Results Conference Call. Today's call is being recorded.

Certain statements contained in this conference call that are not descriptions of historical facts are forward-looking statements, such as terms defined in the Private Securities Litigation Reform Act of 1995. Because such statements can involve risks and uncertainties, actual results may differ materially from those expressed or implied by such forward-looking statements. Factors that could cause results to differ materially from those expressed or implied by such forward-looking statements include but are not limited to those discussed in the filings made by the company with the Securities and Exchange Commission. Many of the factors that will determine the company's future results are beyond the ability of management to control or predict. Listeners should not place undue reliance on forward-looking statements, which can reflect management's views only as of the date hereof. The company undertakes no obligation to revise or update any forward-looking statements or to make any other forward-looking statements, whether as a result of new information, future events or otherwise.

For opening remarks and introductions, I'd now like to turn the call over to ALLETE's Chairman and CEO, Alan R. Hodnik. Please go ahead.

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Good morning, everyone. Thanks for joining us today. With me are ALLETE's President, Bethany Owen; Senior Vice President and Chief Financial Officer, Bob Adams; and ALLETE's Vice President, Controller and Chief Accounting Officer, Steve Morris.

Before I begin our call this morning, I want to again congratulate Bethany Owen on her election by the ALLETE Board of Directors to President of ALLETE. ALLETE has always had a strong talent development process and pipeline. This planned succession process and action by the board is a clear demonstration of those embedded values. Bethany was also recently elected to the ALLETE Board by its directors. I will remain ALLETE's Chairman and CEO and look forward to partnering with Bethany and the entire senior team as we collectively keep ALLETE well positioned, executing various growth strategies and delivering shareholder value.

This morning, we reported full year 2018 financial results of $3.38 per share on net income of $174.1 million. These results are fully consistent with our previously issued 2018 earnings guidance and reflect a year of many accomplishments. Necessary rescaling of Minnesota Power and ALLETE certainly brought challenges for our team. However, our talented employees across all business units stayed focused and delivered outstanding safety, operational and financial results. ALLETE will be 113 years young this spring, and I could not be more proud of the way we have and continue to answer the call to transform the nation's energy and water landscape while growing ALLETE.

Before Steve and Bob take you through the details of our 2018 financial results and 2019 earnings guidance, I wish to highlight a few of the many accomplishments achieved during the year.

Minnesota Power has been hard at work for years, balancing multiple stakeholder interests while executing its Energy Forward strategy. With support from state policy and regulatory leaders, Minnesota Power has effectuated the thoughtful retirement of 700 megawatts of coal, resulting in a material reduction of greenhouse gas and other emissions, and a sizable expansion of renewable generation all while modernizing its delivery system. Major construction advanced on its Great Northern Transmission Line, which will be ready to move carbon-free hydro power into the MP service territory as early as June of next year. Manitoba Hydro is, of course, still working on their end of the line.

Another transforming EnergyForward initiative, the Nemadji Trail Energy Center was also approved late last year by the Minnesota Public Utilities Commission. NTEC represents the first natural gas source generation in Minnesota Power's portfolio and will support additional renewable generation while assuring grid reliability.

Late in 2018, renewable energy expansion within the company experienced another major 250-megawatt leap forward as the Nobles 2 wind generation project received approval from the Minnesota Public Utilities Commission. The Nobles 2 initiative is designed to deliver carbon-free energy to MP customers for decades to come.

As recent as 2005, Minnesota Power was a 95% coal-dominated utility. Given its relative start point, EnergyForward has propelled Minnesota Power farther and faster than many other utilities in the Upper Midwest.

In terms of carbon reduction, MP anticipates being 45% renewable by 2025, well ahead of Minnesota's 25% by 2025 standard. Given its geographic positioning to wind-rich North Dakota and water-rich Canada, including transmission superhighways to both, Minnesota Power is well positioned to deliver an even more sustainable energy future ahead.

On the customer front, Minnesota Power's taconite customers finished 2018 at near-full production, and it anticipates continued strength in 2019. A strong economy and trade protection has resulted in high levels of production, along with significant customer investment in the respective iron ore and steel-producing facilities. These actions support our view that Minnesota Power's natural resource-based service territory here in Northeastern Minnesota has a bright future.

ALLETE Clean Energy experienced a year of significant project construction and fleet optimization. ACE highlights include the completion and sale of the Thunder Spirit wind energy facility; the establishment of a new customer and long-term wind energy power sales agreement with NorthWestern Energy in Montana; ongoing refurbishment activities on its own wind generation fleet; securing its first major contract extension with Northern States Power, Xcel Energy, in Minnesota; and beginning preliminary work on large wind generation projects that will ramp into robust construction mode with targeted completion for later this year.

ALLETE Clean Energy's safe harbor turbines are a key differentiator for the company, thereby providing a unique opportunity for ALLETE Clean Energy to materially expand its operations and earnings base. ALLETE Clean Energy has many paths for multi-year growth, has maintained its financial discipline and its deal pipeline remains robust. They remain busy negotiating potential new customer power sales agreements while pursuing additional projects for the future. 2019 will be an exciting year for ALLETE as we see opportunities for our continued clean energy progression to be as robust as ever.

On a different note, last Friday, we announced the execution of an agreement to sell our interest in U.S. Water Services for a cash purchase price of $270 million. As we emphasized, this transaction provides a timely opportunity to reposition and refocus ALLETE's growth initiatives on cleaner energy for the future.

We will continue to execute on our multifaceted, multi-year growth strategy and believe our unique business mix will continue to deliver a strong value proposition to shareholders for the longer term. The ALLETE Board recently demonstrated its confidence in our strategy and the future by raising the dividend; this, for the ninth year in a row. We will remain financially disciplined as our future dividend increases are expected to align with our long-term earnings growth and strong cash flow.

Bethany Owen will provide some additional 2019 perspective shortly, and I will provide an update on other key initiatives and developments later in the call.

But first, I will ask Steve and Bob to go through the 2018 financial results and the 2019 earnings outlook.

Steve?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Thanks, Al, and good morning, everyone. I would like to remind you that we filed our 10-K this morning, along with an 8-K that provides details of our 2019 earnings guidance. I encourage you to refer to them for more details.

For the year ended 2018, ALLETE reported earnings of $3.38 per share on net income of $174.1 million. Earnings in 2017 were $3.38 per share on net income of $172.2 million. Earnings were diluted by $0.04 per share in 2018 due to additional shares of common stock outstanding at year-end.

Before I discuss segment details, I will call out significant year-over-year timing variances and other items for comparison consideration. We have included further details of these items in our first 4 slides for your reference at our website at allete.com in the Investor Presentation section.

Recall that results for 2017 reflected a $13 million after-tax or $0.25 per share benefit for the remeasurement of ALLETE's deferred income tax assets and liabilities resulting from the Tax Cuts and Jobs Act that was enacted in December of 2017. Net income for 2017 also included a benefit of $7.9 million after tax or $0.16 per share for the favorable regulatory decision on the allocation of North Dakota investment tax credits. These favorable impacts were partially offset by a noncash $11.4 million after-tax charge or $0.22 per share in 2017 for the write-off of a regulatory asset for deferred fuel adjustment clause costs due to the anticipated adoption of a forward-looking fuel adjustment clause methodology.

Interim retail rates recognized in 2018 of approximately $30 million pretax were fully offset by a corresponding reserve recorded throughout the year. In the fourth quarter of 2017, Minnesota Power recorded interim retail rate refund reserves of approximately $32 million pretax to fully offset interim rates recognized throughout the year in 2017. From a full year-over-year comparison, there was no impact on our financial results from interim rate refund reserves.

A few details from our business segments. ALLETE's Regulated Operations segment, which includes Minnesota Power, Superior Water, Light and Power and the company's investment in the American Transmission Company, recorded net income in 2018 of $131 million, an increase of $2.6 million compared to 2017. The 2017 net income reflected the previously mentioned $11.4 million after-tax charge for the write-off of our regulatory assets for deferred fuel adjustment clause costs. Net income for Regulated Operations decreased in 2018 due to lower transmission revenue, fuel adjustment clause recoveries, industrial sales and higher property tax and interest expense. These decreases were partially offset by lower operating and maintenance expense, higher pricing on power supply agreements with other power suppliers, increased cost recovery rider revenue and higher kilowatt hour sales to residential and commercial customers due to more favorable weather conditions in 2018.

Net income in 2018 also included higher depreciation expense resulting from the reduction in the depreciable lives of Boswell units 3 and 4 to 2035, which was offset by the benefits of the lower federal income tax rate resulting from tax reform. Net income at Superior Water, Light and Power and our after-tax equity earnings in ATC were similar to 2017.

Net income at ALLETE Clean Energy decreased $7.8 million from 2017. Net income in 2017 included a $23.6 million after-tax benefit due to the remeasurement of deferred income taxes resulting from tax reform. Net income in 2018 included the sale of a wind energy facility to Montana-Dakota Utilities, resulting in an after-tax profit of approximately $10 million or $0.20 per share. ALLETE Clean Energy recognized $7.4 million of additional production tax credits as it continues to execute on its refurbishment strategy. These increases were partially offset by lower revenues due to lower wind resources, primarily at its Midwest facilities, and higher operating and maintenance expenses.

U.S. Water Services' net income decreased $7.5 million from 2017. Net income in 2017 included a $9.2 million after-tax benefit due to the remeasurement of deferred income taxes resulting from tax reform. Net income in 2018 included increased revenue, partially offset by higher operating expenses.

Turning to the fourth quarter of 2018. ALLETE reported earnings of $1.18 per share on net income of $61.1 million. Earnings in the -- for the fourth quarter of 2017 were $0.81 per share on net income of $41.4 million. The fourth quarter of 2017 included the previously mentioned benefit for the remeasurement of deferred income taxes of $0.25 per share and the write-off of our regulatory asset related to deferred fuel adjustment clause costs of $0.22 per share. The fourth quarter of 2017 also included recognition of a full year of interim rate refund reserves, of which approximately $14 million after tax related to the first 3 quarters in 2017. In 2018, interim rate refund reserves were recorded throughout the year.

Depreciation expense also decreased in the fourth quarter of 2017 due to the Minnesota Public Utilities Commission's decision to increase the depreciable lives of Boswell units 3 and 4 to 2050, resulting in lower depreciation expense of approximately $14 million after tax. In 2018, the Minnesota Public Utilities Commission reduced the depreciable lives of Boswell units 3 and 4 to 2035. The increase in depreciation expense in 2018 was offset through the use of the lower federal income tax rate enacted as part of tax reform.

Other significant variances from a quarter-over-quarter comparison include ALLETE Clean Energy's sale of a wind energy facility, resulting in earnings of $0.20 per share and an increase in U.S. Water Services' operating income due to higher capital project sales. Capital project sales amounted to approximately $15 million pretax in the fourth quarter of 2018.

I'll now hand it off to Bob for additional comments on our 2018 financial performance and 2019 guidance. Bob?

Robert J. Adams *ALLETE, Inc. - Senior VP & CFO*

Thanks, Steve, and good morning, everyone. Let me begin by saying how proud I am of ALLETE's 2018 performance. Not only did we meet the financial promises we made to our investors, coming in a bit north of our 2018 midpoint EPS guidance, we also advanced several major strategic initiatives, which will set the stage for added growth, cash flow generation and optionality as we go forward.

First, we materially completed a historic rescale of Minnesota Power's operating structure, reducing cost for customers, increasing returns earned for investors while still maintaining our high standard for safety and reliability. Second, we announced 3 major new clean energy investments and additional refurbishment opportunities at our Regulated and Nonregulated segments as we continue to execute on ALLETE's overall sustainable, cleaner energy forms thesis. The investments included South Peak, Nobles and NTEC, collectively representing approximately $650 million in total investment. As illustrated on the slide titled Schedule of Capital Expenditures, we have over $1.8 billion in total spend scheduled for the next 5 years, of which clean energy projects represent the vast majority, as highlighted. These clean energy projects will provide an opportunity to invest approximately $300 million of additional equity during the 2019 through 2023 time frame.

Finally, as announced on Friday of last week, we reached an agreement to sell our industrial water services company, U.S. Water, for a significant premium. The cash proceeds of which will now be redirected to fund other clean energy growth initiatives, opportunities we are confident will materialize throughout the year. Specifically, the sale price was $270 million, which would result in an estimated gain of approximately $20 million pretax upon closing. The transaction will generate approximately $260 million of net cash proceeds and is expected to close in the first quarter of 2019. We expect that this action will increase our overall credit headroom as we seek to accelerate our growth at ALLETE Clean Energy, a business which has demonstrated higher returns, less earnings variability and stronger cash flows than U.S. Water.

Going forward, we are excited about our ability to increase our annual dividend from $2.24 to $2.35 per share, a healthy 5% increase over 2018, fulfilling our goal that future dividend increases would more closely match our 5% to 7% average annual earnings growth objectives while maintaining healthy dividend payout ratios.

ALLETE is a much stronger company as we enter 2019, with multi-year growth drivers already in place at ALLETE Clean Energy; a solid pipeline of additional opportunities yet to be announced; and on a platform of solid fundamentals, including improving returns from all of our businesses; significant free cash flow generation, which can be used to fund new initiatives; a strong balance sheet, supported with low leverage; increased credit headroom, which will enable further nonregulated growth; and an improvement in overall earnings quality, measured in terms of reduced variability.

Consistent with this view and as we look forward to the next 5-year time frame, we are upward revising our average annual growth expectations for the Regulated segment to be approximately 4% to 5% from the 3% to 4% previously communicated, reflecting improved returns and added investments on our DC transmission line to increase the capacity with the assumption of reasonable regulatory outcomes.

Our nonregulated segment average annual growth is projected to increase at least 15%, reflecting our recently announced $170 million investment in Nobles 2 and our confidence in added wind projects from ALLETE Clean Energy. These growth rates appropriately exclude any contributions from U.S. Water given the previously announced divestiture.

Indeed, our 2019 guidance, which I will review in a moment, reflects an increase of over 8% above 2018 results, exceeding our 5% to 7% annual average objective when normalized for both the gain and the U.S. Water sale gain in 2018 and 2019, respectively.

As we look forward to 2020, we expect this strong growth to accelerate even further as 2 of ALLETE Clean Energy's newest wind farms, Glen Ullin and South Peak, representing approximately $300 million in total investment, are in service for the full year in 2020.

So now let's get on into more specifics of our 2019 guidance. In 2019, we expect to generate a range of $3.50 to $3.80 per share on net income of $180 million to $190 million, which includes an expected gain on the sale of U.S. Water of approximately $10 million after tax or $0.20 per share. This guidance range is comprised of Regulated Operations segment earnings within a range of $2.85 to $3.05 per share and ALLETE Clean Energy and Corporate and Other earnings within a range of $0.65 to $0.75 per share, which includes the U.S. Water Services gain of $0.20 per share.

I would ask that you refer to the slide titled 2019 Guidance Highlights for further reference and our full 2019 guidance 8-K details filed with the SEC early this morning.

I'll share a few other factors and assumptions from our guidance starting with our Regulated Operations. We expect additional cost recovery revenue from the Great Northern Transmission Line capital investments, with Minnesota Power's portion of the anticipated expenditures estimated at $127 million in 2019. Industrial sales for Minnesota Power expected to be approximately 7 million to 7.5 million megawatt hours, reflecting taconite customer production levels of approximately 39 million tons. As we project forward to 2020, Minnesota Power will realize a significant reduction in revenue associated with expiring power sales reduced transmission revenues. In addition, we would expect normal expense increases in the future with inflationary pressures. Given the significant revenue deficiencies, we do anticipate the need for -- to file a rate case in late 2019, and we will be sharing more information as 2019 progresses as it relates to the timing and approach plus potential impacts in 2020.

Additional investments in American Transmission Company of approximately $9 million, which is on top of our 2018 year-end balance of $128 million, earning an attractive ROE of 10.82%.

A few highlights from our 2019 guidance regarding ALLETE Clean Energy and Corporate and Other. We continue to be excited about future growth prospects for ALLETE Clean Energy as it executes on its 4-prong growth strategy that at a high level includes: optimization of existing facilities; building, owning and transferring facilities to others; building, owning and operating facilities under long-term power sales agreements; and acquiring additional renewable facilities. Our guidance excludes the impact, if any, of possible acquisitions or new additional development projects.

ALLETE Clean Energy expects to generate approximately 1.5 million megawatt hours versus 1.2 million megawatt hours in 2018, with return of normal wind resources and South Peak and Glen Ullin projects coming online in late 2019. ALLETE Clean Energy expects additional business development expenses plus added staffing as well as higher depreciation expense. ALLETE Clean Energy is investing in its future with additional staffing that will enhance origination, development and back-office support as needed for orderly scaling as it further expands its operations.

We expect to spend approximately $22 million in requalification of wind turbine generators in 2019. Production tax credits related to these refurbishment projects are estimated to be approximately $14 million in 2019.

I would encourage you again to review the complete 8-K disclosure filed this morning, which includes additional details of our 2019 guidance. As we look forward, I'm excited about the prospects for all of our businesses at ALLETE. We believe these businesses provide a differentiated mix of long-term earnings and cash flow growth potential as well as balanced exposure to our regulated industrial customers. We are, indeed, in an exciting chapter at ALLETE.

Al?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Well, thank you for the financial updates, Steve and Bob. ALLETE is an energy company with a differentiated strategy, a strategy that brings about cleaner energy solutions through initiatives underway within our regulated and nonregulated family of businesses. We continue to see growth opportunities, primarily driven by the call to upgrade our nation's infrastructure, to transform its energy supply and to further electrify its broad economy. Minnesota Power's strategic EnergyForward plan has done just that, greatly transforming its overall energy platform with significant rate-based investments in cleaner generation, carbon-free renewables and modernizing transmission projects. As expressed earlier, the Nemadji Trail Energy Center, a partnership between Minnesota Power and Dairyland Cooperative, successfully completed a major regulatory hurdle in Minnesota as its capacity dedication agreement was approved by the Minnesota Public Utilities Commission in a final order dated January 24, 2019.

Action has now shifted to the state of Wisconsin as an application for public convenience and necessity was submitted to the Public Service Commission of Wisconsin on January 8, with a final decision expected in 2020.

In regards to Minnesota Power's companion filings, filings that are part of its EnergyForward energy resource package, we were pleased that the 20-year, 250-megawatt Nobles 2 wind power purchase agreement was approved by the Minnesota Public Utilities Commission in an order dated January 23, 2019.

In addition to the Nobles 2 power purchase agreement, our wholly owned subsidiary, ALLETE South Wind, entered into a partnership with Tenaska to purchase a 49% equity interest in Nobles 2, providing an attractive investment opportunity for ALLETE, yet another great example of the creativity of the talented ALLETE team.

I would like to make a comment on a new natural resources customer that is staged to begin production in the next 2 years. PolyMet's proposed copper, nickel and precious metal mining operation in Northeastern Minnesota continues to report advancement on major permitting milestones. During 2018, PolyMet received its permit to mine and certain water-related permits from the Minnesota Department of Natural Resources. And on December 20, 2018, the Minnesota Pollution Control Agency issued PolyMet's final state water and air quality permits. The final records of decision by federal agencies is required and expected in 2019 before final action can be taken on required federal permits as they relate to financing, constructing and ultimately operating the first in Minnesota history nonferrous mining operation.

I will now turn it over to Bethany Owen for a few more comments on our renewable energy business and outlook for the future.

Bethany?

Bethany M. Owen ***ALLETE, Inc. - President & Director***

Thanks, Al. I couldn't be more excited about ALLETE's future, and I'm honored to work with Al and his talented team as together we lead this world-class organization. 2019 is a year of strategic positioning at ALLETE as we continue to execute on our growth strategy. With an anticipated Minnesota Power rate review in 2020 an historic level of capital projects underway at ALLETE Clean Energy and the announced sale of U.S. Water Services, the proceeds of which are expected to be used to further ALLETE's growth strategy, we are moving forward from a position of strength.

At our regulated business across the bay, Superior Water, Light and Power continues to enhance the reliability and safety of electric gas and water services for its customers while growing its business. We were pleased that its 2018 rate case was approved at the end of last year, with final rates going into effect on January 1 of this year. Superior Water, Light and Power anticipates another year of significant capital investment, approximately $15 million in 2019.

As Bob highlighted a moment ago, 2019 will be a monumental year with a record high level of PTC-related construction activity at ALLETE Clean Energy. Upon completion of the South Peak and Glen Ullin projects, ALLETE Clean Energy will have close to 750 megawatts of carbon-free renewable wind generation in operation, resulting in significant growth for ALLETE in 2020 and beyond.

We anticipate additional opportunities for growth at ALLETE Clean Energy with the advent of higher renewable standards across the country over the next several years. The demand for carbon-free and renewable energy is staged for multi-year growth since only 29 states thus far have well-established renewable portfolio standards. In addition, most of those 29 states are expected to increase their renewable requirements over time. ALLETE Clean Energy is ready and able to capture a meaningful share of this opportunity. The company's current operating and development portfolio includes 60,000 acres of land and access rights, 300 landowner relationships and more than 700 megawatts of interconnection rights, along with permits already in hand.

This is truly an exciting time for all of us at ALLETE as we continue to demonstrate our commitment to sustainability. We look forward to great opportunities for our employees, excellent service for our customers and delivering value to our shareholders through earnings growth and dividends. We believe ALLETE's diversified growth platform and our proven ability to execute offer an attractive and differentiated value proposition to investors.

Thank you for your interest and for your investment in ALLETE. At this time, I will ask the operator to open up the line for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Chris Ellinghaus with Williams Capital.

Christopher Ronald Ellinghaus ***The Williams Capital Group, L.P., Research Division - Senior Equity Research Analyst of Power and Natural Gas***

Hey, Bob, I've got a -- I was particularly interested in the final slide where -- in the CapEx, there's the DC line upgrade. I assume that includes the capacity expansion. And can you just sort of talk about what's changed there? And can we infer that there's additional projects out west that necessitate that?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes, so very good question. I -- Chris, you'll recall, this is something that we've been evaluating for a while. Recall that the DC line capacity is -- current capacity is a little over 500 megawatts. And that provides a very unique path, a very high-quality wind in North Dakota, that particular line. And so we've been in the schedule now. We are contemplating upgrading the capacity by about 200 megawatts. And so there's about a $50 million incremental capital that would be on top of approximately $200 million that we would otherwise be doing just to modernize the path. And so it will -- we are definitely bullish on what that will mean, that additional capacity for additional projects. Again, it is unique. And keep in mind, the Midwest itself as we look forward is still looking at another 8,000 megawatts of wind. And so we're pretty excited about it.

Christopher Ronald Ellinghaus ***The Williams Capital Group, L.P., Research Division - Senior Equity Research Analyst of Power and Natural Gas***

Okay. The Nemadji line, the CapEx, does that suggest that it's complete in 2023?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

It is not quite complete. I believe, Steve, you can correct me here, that it goes into service in early 2025, NTEC?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

2025, there's some small capital, Chris, that's outside of the schedule in 2024. And then there's some testing, obviously, in mid-2024, with a start date expected very early in 2025.

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Chris, this is Al. That assumes, of course, that permitting in the state of Wisconsin goes as we anticipate, and also, obviously, within MISO that the MISO queue is as we anticipate. But that's kind of our projections right now.

Christopher Ronald Ellinghaus ***The Williams Capital Group, L.P., Research Division - Senior Equity Research Analyst of Power and Natural Gas***

Okay. Al, as far as PolyMet goes, what's the current thought process in terms of starting construction and what the construction timeline looks like?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Well, I can only speak to what the company shared online and on the website. I would say, what's still needed from the permitting side is the permit from the Army Corps of Engineers. That got a little bit stymied by virtue of the government shutdown that ensued in January, February kind of time frame. The U.S. EPA had an obligation to do a final review of that Army Corps permit. So the company is waiting for that to come in. Once we have that permit, we have all the permits, they would move into kind of solidifying their financing. The construction schedule, as Steve outlined, it is anywhere from 18 to 20 some months. So you can kind of extrapolate from there and based on when the financing comes into play. So they are suggesting within a 2-year time frame, they would be up and operating. It could be plus or minus that.

Christopher Ronald Ellinghaus ***The Williams Capital Group, L.P., Research Division - Senior Equity Research Analyst of Power and Natural Gas***

Okay. And Bob, one last question. As far as the U.S. Water equipment sales in the fourth quarter, was that the total of what you were expecting might be pushed into the first quarter?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes. Actually, we had about $15 million that we had planned in the fourth quarter, and all of the $15 million did end up shipping. So we had a little bit of slippage, $1 million or $2 million that we had thought we could even pull into the fourth quarter, but overall, it turned out to be a fair outcome.

Operator

Our next question comes from Lizzie Guynn with Mizuho.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Could you clarify what the base is for the 5% to 7% growth rate?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

So that is an average annual range. Within that range, as I expressed here this morning, we are looking at the utility, the regulated side of the business, if you will, which should include Superior Water, Light and Power, growing at a rate of 4% to 5% on average. So we've increased that from 3% to 4%. And then...

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

And sorry, that's 4% to 5% off of the 2018 actual? Or off of the 2.55% midpoint?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

That would be off the midpoint.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Okay. Perfect. And then at unregulated business?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes. So on the unregulated piece, as you will recall, we have talked about that segment growing at about 15%. And the difference maker here, of course, at the time, we had expressed 15% last year and in prior years as we had U.S. Water in the mix. So this is back to what we talked about before, which is we feel confident now that without U.S. Water, we can maintain that 15% growth, in part, that is being fueled by our Nobles investment now that we just announced that will be done in the 2020 time frame. And we are also expecting additional growth from ALLETE Clean Energy.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Great. So is that 15% off of the $0.80 minus the $0.20 onetime gain on the ACE sales so really, 15% off of a base of $0.60 EPS?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

That's correct.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Okay, great. So then on a consolidated basis, we can think of the 5% to 7% off of a $3.18 base?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

That's correct.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Or actually, the $3.15 because the ACE sale is actually $0.20. So it's the $3.35 minus the $0.20 ACE sale.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

I'd use -- this is Steve. I'd use our $3.38 actual, take off the $0.20 and get to $3.18.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Okay, perfect. But we shouldn't use the actuals at the different segments?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Well, I think you got to account for -- on the nonreg side, you need to, obviously, back off the MDU, the $0.20 from that, too. So it was -- I believe in '18, it was $0.84. And so I think you need to back off the MDU sale of that as well.

Elizabeth Roi Guynn ***Mizuho Securities USA LLC, Research Division - Assistant VP***

Okay. So it would be the $0.84, but they should really be off of an EPS of $0.64 at the unregulated.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes. I would look at that, and so that also included $0.06 for U.S. Water, which we won't have in 2019 as well. So keep that in mind. And that's why you heard on this call, we talked about positioning for 2019 with significant growth in 2020, right? So well have 2 new projects in line late 2019, so factor that in. So it's 5% to 7% average annual earnings growth.

Operator

Our next question comes from Paul Ridzon with KeyBanc.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

Question on -- you talked about the refurbishment in '19 adding $14 million to production tax credit. Is that $14 million incremental to the $7.4 million in '18? Or is that $14 million in total?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

That's $14 million in total, Paul.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

Okay. So kind of basically doubling what you did in '18.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes. So it includes Congdeon, and then as you know, as you do wind turbines, they go online and generate PTCs right away. These projects are expected to be complete mid-2020. So we would have, obviously, some incremental from whatever we recognized in 2018. It was actually around $8 million-some. So it's probably an increase of about $6 million overall.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

And then in the past, you've shared with us how many megawatts of RFPs you bid into ACE. Is there a current number there?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes, Paul, that's still around 1,500 to 1,600 megawatts.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

Okay. And then how are you looking at -- I don't know what we're calling it now, Essar, Mesabi Metallics, kind of what -- can you just give us an update on what's going on there, the prospects for loads and that?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Sure, Paul. So you probably read in the paper that the state of Minnesota has taken action -- there's a new governor here, Governor Walz. He's taken action right now through his Attorney General's office and the Department of Natural Resources and issued a debarment notice to Essar, essentially, or those -- that entity that come back into Minnesota to finance and play a role in the project. So that's kind of underway right now, and we'll see how that kind of proceeds at this point in time. The company, of course, has a contract with the city of Nashwauk through 2032. There was talk that Metallics, as we knew it, would begin construction in the spring. I think they are still representing that they will do that. I think the jury is out on there right now. And of course, the state of Minnesota, as I've told you, has issued that debarment sort of proceeding to no longer declare them, if you will, acceptable to do business in Minnesota. So that's where it sits in the moment. I probably have more to say about that in the spring as winter gives way to spring here, and we'll see what actually happens on the ground there. But that's still about 100 megawatts, 120-megawatt load for the company. The project is essentially half finished right now. And Cleveland-Cliffs, of course, still has a strong interest in the property. And they have said to the governor, again, at this point in time, that they would very much be interested in the property. And of course, they would like to do some value added here in Minnesota as well over the HBI pieces. And so Cliffs is also sort of in the mix and the conversation right now, and we'll see how it all plays out.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

So if you were a gambling man, in what odds would you put that you'll be selling them power in 2 years?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Well, I don't want to speculate on that. I would be a liar and would lose all my money because this has been going on for 10 years already, Paul. So I'm not going to speculate there with regards to that. But I feel fully confident that it will ultimately get up and running. As I said to you all many, many times, that is one of the last remaining sort of sizable and untapped ore bodies. Cleveland-Cliffs has a sizable ownership stake right now in -- by virtue of the actions they took about 1.5 years ago. And so that ore body is very attractive. It's got the right mineralogy. It's got the right softness, if you will, with respect to ore and ore grinding. And it's very good and very conducive right now by virtue of its characteristics for enhanced HBI-type products. And so everybody wants that ore and everybody wants that project over there in the state. Just got to clear the depths and all the complexities that it had created during Governor Dayton's administration and/or the court has created by virtue of people coming in and out of bankruptcy.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

The midpoint of your Regulated Operations guidance for '19, what's the assumed earned ROE in that?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

All right. The $2.85 to the $3.05, Paul?

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

Yes, sorry.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes. I would use the midpoint on that.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

At that midpoint, what is the assumed ROE, sorry?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes. It's -- as we talked, Paul, it's 9.05%. So that's our -- we use our authorized ROE at 9.25%, and of course, we've been on a rescaling for Minnesota Power. So as we've talked, we have achieved that with a caveat of the temporary outage at Husky. That's about a $3 million impact in 2019, they don't believe they'll be up and running until sometime in 2020, or about 20 basis points. So I take the 9.25% minus the 20, it's a 9.05% ROE.

Paul Thomas Ridzon ***KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst***

So you scaled your own to hit the 9.25%, what we have as headwind?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes, exactly.

Operator

Our next question comes from Christopher Turnure with JPMorgan.

Richard Wallace Sunderland ***JP Morgan Chase & Co, Research Division - Analyst***

It's actually Rich Sunderland on for Chris. Just -- a lot of great questions today. Just want to ask on the rate case, and I know we're a little early here. But the contract expirations that you referenced, how can we think about the deal impact from those? And just maybe some other high-level puts and takes on the direction of rates.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes, I can help with that. So I'd start by saying we are working on our 2020 forecast right now, which is going to take some time, so we aren't coming out with saying, hey, how big of this rate case it is. So we need to work through that. We would expect to have that probably by the early third quarter of 2019. So it's a little too early to get into how much and what the impact on rates are. And Bob mentioned some of the reasons for this rate case because we do have some expiring contracts with power marketing customers, some transmission revenue that we had that came offline right during the rate case that we were not able to get into that rate case. We had a customer -- a paper customer shut down one of their smaller of their paper machines, which we did not have in this rate case. Potentially, a Manitoba Hydro contract that we have that could start on -- roughly on June 2020, that could come into play. We also expect higher expenditures. So we've done a lot of cost reduction, that is not sustainable over a long term. You've seen the CapEx schedule that we have as well as what we believe is -- will be our improving ROEs in Minnesota.

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Rich, this is Al. With respect to contracts and rates for large customers, if that's what you're referencing, are in general, we're feeling very good about where our rate structure is at the moment. When you marry that up with all the transformative work that Minnesota Power has done or has been required to do in the state of Minnesota, to mercury reduction, to clean energy expansion and renewables, to grid security and reliability with respect to transmission upgrades, when you add all that up, we moved Minnesota forward, we move Minnesota energy policy forward, and we've kept our rates reasonable for the most part. The large power customers' rates have come down modestly since the rate case and since the Trump tax reform and other things that had impacted them. And of course, trade policy and a strong economy is lifting them as well. And so we have good solid relationships right now with our big customers. The model remains with our Essar situation or Metallics situation, as I described earlier, that load has been up and down by virtue of kind of bankruptcy and whatnot. But the contract there is solid, and we look forward to serving that load to the city of Nashwauk, a muni customer of ours that we've had a long-standing relationship with. So right now, I would say, we're positioned well, both in terms of our customers' rates and also planning for rate case filing sometime later this year.

Richard Wallace Sunderland ***JP Morgan Chase & Co, Research Division - Analyst***

Got it. And just a quick one final here. On -- as for interim rates, do you implement the ROE you file? Or is it the ROE you're currently authorized when you get there?

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Yes, it depends. Generally, if it's lower, you would have a lower interim that would result in lower interim rate, you would use that. If it's higher, generally not.

Operator

The next question comes from Vedula Murti with Avon Capital.

Vedula Murti

A few things here. One, can you just remind me what's the anticipated net income earnings contribution from the PolyMet facility when it comes online, I think, it's in 2022?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

We don't get into kind of gross or net numbers around all that. The 50-megawatt expected load we cited in our 10-K, Steve can highlight this, what -- roughly a ton of taconite is, but copper nickel is slightly different.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

So we've used about $0.04 per 1 million ton increase or decrease.

Vedula Murti

Okay. And that's 5 million tons?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Well, the average taconite production on the Iron Range is 40 million tons, and so that's about the average of that. Of course, PolyMet would be the first of a kind in Minnesota history, and its production right now is -- the permitted production is 32,000 tons of production per day. So it's a little difficult, but think about taconite at 40,000 -- 40 million tons per year, excuse me, Steve's reference there of plus or minus $0.04 based on -- up or down based off that production rate.

Vedula Murti

So every 1 million tons is plus or minus $0.04.

Steven Wayne Morris ***ALLETE, Inc. - VP, Controller & CAO***

Correct.

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

In taconite.

Vedula Murti

Yes. When you talked about your growth outlook and guidance, I was looking at the capital expenditures slide. And it appears that there's -- especially within ALLETE Clean Energy, except for what has already been specifically identified with regards to doing power refurbishments and Glen Ullin, I think there's nothing else included in there right now. And I have seen that the growth rate is consistent with the capital forecast that's here such that as you back fill in capital opportunities over the next 3, 4 years on this plan, that then, in fact, should be additive to where we are today and would be on top of what you'd see as a 15% growth rate.

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes, so Murti, this is Bob. This goes back a little bit to our conservatism as a company, I would say, too. When we put these CapEx schedules out, these do not include projected new projects, if you will. Now we do have -- I already mentioned in the DC line, it's -- these are high confidence kinds of things as it relates to the upgrades. But in the absence of that, these are established projects. So we would certainly be looking to add additional projects at ALLETE Clean Energy. You may recall our target has been 1 to 2 projects per year. And we would need the 1 to 2 projects per year to get to the growth rate overall. So we're going to need to and are working on projects, for example, that would come in the 2021 through 2023 time frame as we move forward.

Vedula Murti

Okay. And I guess given the incremental capacity that you've been able to achieve on your balance sheet in addition to the cash from the sale of U.S. Water, can you give me a sense as to what you would consider realistic amount of firepower you would have or dry powder now so to speak in terms of capital to be effectively deployed going forward here?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes. So I would start with the fact that our business, overall ALLETE, now generates about $50 million to $70 million on average in equity free cash flow. So that's net of dividend and base capital expenditure. So that is a source of capital that we would look to redeploy. For example, if we did a 100-megawatt new wind farm, that's about a $50 million equity check. So we don't have to raise equity in that circumstance. We could use the cash flow just for that. So that's a big benefit. Now on top of that, of course, now we have these proceeds from U.S. Water, and we have our eyes set on what I consider to be a pretty robust pipeline that the ACE team is working on, and we would look to dedicate a significant amount of those proceeds to offset equity that we would otherwise issue in those projects.

Vedula Murti

Yes, it seems to me that with the -- you highlighted particularly in 2018 versus 2017 all normalized that you were able to grow at an 8% growth rate. And given the outlook for the utility as well as the opportunities at ACE, it would seem to me that what you were able to achieve in '18 versus '17, that should be perhaps more indicative of what you're able to achieve going forward. So I wondered, are you coming there? Or is it simply a matter of conservatism in that you're keeping 5% to 7% simply to be conservative plus to -- the fact that '18 versus '17 was about 8%, and it seems like you have a lot of pieces in place to be able to continue to that.

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes. So Murti, I appreciate that comment. We pride ourselves on performing. So what we say we're going to do, we're hell-bent on making sure that happens. So let me just start with that. With regard to the 5% to 7%, recall, that's a long-term average growth rate. And for sure, as you pointed out, as we look at our guidance for 2019, we're at 8%. I've already hinted towards 2020 is going to be at a higher rate than that because of these projects coming on. So there will be years that we're going to outperform. But as we look longer into the period, and I think this is where the conservatism comes, we have more work to do. And I'm talking over the -- even past 5 years, we feel really good about our growth at the higher end of that range over the next 5 years. And so we're really working on that next 5-year period and want to make sure that we can consistently deliver that range, that 5% to 7%, which we think we can.

Vedula Murti

And then just last one. We have an Analyst Day here in the next month. What do you expect incremental that you will be able to communicate or hope to communicate?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Well, I would tell you this, and maybe Al would like to comment as well or Bethany. I -- we're going to have Al Rudeck joining us from ALLETE Clean Energy once again. He was there last year. And he is going to provide -- he'll have more time on the agenda. He is going to be providing more color with regard to how they're looking at the business more broadly. Recall, they're evolving their strategy as we speak. Some of the things that Steve spoke to, I spoke to in my script about ramping up the back office, new origination resources, operational folks is about a continued scaling of that business. So he'll speak to that at significant length. Al?

Alan R. Hodnik ***ALLETE, Inc. - Chairman & CEO***

Yes, no, he'll be addressing all of that. Of course, last year, we had a timing work out for us with respect to the NorthWestern deal peak. We announced that out there at the breakfast. We don't necessarily always control our timing and our market timing that way. But we are confident and bullish about ACE's future and its ability to get more projects done. As I suggested earlier, they're in various stages of negotiation on power sales agreements with a variety of customers. They don't always work out, but we're confident we're going to get our share. And as Bethany pointed out earlier, we've got 30 states right now with mandates and maybe more coming, not only within those states but other states. And so we believe that ACE will be and is well positioned to claim its share of the business. And as Bob already suggested, from a balance sheet perspective, the company is generating a fair amount of cash right now. We have no access to capital challenges at all. We're very financially disciplined. We're very return disciplined, and so we don't just chase every deal down and race to the bottom. That's not our strategy. And so we're very deliberate and very intentional. So we'll have more to say in New York when we're with you and more throughout the year. So ALLETE's got a lot on the ground right now. I'll just leave it in there..

Vedula Murti

And I guess maybe one last thing. You did reference perhaps equity buybacks. I mean, I guess given the opportunities that you're seeing right now, would any stock buybacks likely be later in the forecast period as you evaluate -- as you target a closer line of sight, if not announced project developments or acquisitions within ACE? Or do you feel that while that's always an option that, in fact, the rate of return from these investments will be materially better than the stock repurchase?

Robert J. Adams ***ALLETE, Inc. - Senior VP & CFO***

Yes. So a lot there. I would tell you that in terms of our cash management philosophy overall, I like to keep a cash balance of around $50 million. So let's start there. When I think of these proceeds in terms of roughly $260 million coming in, I want to make sure that we were good stewards of that cash. So I don't look at this as sitting on that cash for an extended period of time. I'm very much focused on the 2019 calendar year. So -- and against the backdrop of $50 million in cash. So we're going to be looking hard in the beginning of the year, call it, the first 3 to 4 months, on projects that could come from ALLETE Clean Energy that would require equity, as I already expressed. We have a very robust pipeline. Those projects could be new development projects, PTC projects or they could be acquisitions of existing facilities. And that would require an equity check. So that's first and foremost. So I'm thinking about that. And then to the extent that as the year progresses we're able to dedicate some of those proceeds to those projects, great. To the extent that we don't see projects, for example, on the last half of the year, we will initiate -- likely initiate a program to start that buyback in the second half. So that's generally how we're looking at it. So I'm not looking out 3 years, 4 years in the context of these proceeds.

Operator

Ladies and gentlemen, this does conclude the Q&A portion of today's conference. I'll turn the call back over to Al Hodnik with closing comments.

Bethany M. Owen ***ALLETE, Inc. - President & Director***

Steve, Bob, Alan and I thank you again for being with us this morning and for your investment and interest in ALLETE. We look forward to seeing many of you at our annual analyst breakfast in New York on March 7 and at other investor venues throughout the year. Enjoy the rest of your day.

Operator

Ladies and gentlemen, this does conclude today's presentation. You may now disconnect, and have a wonderful day.