ALLETE

Moderator: Al Hodnik
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Operator: This is conference # 87733201.

Operator: Good day, ladies and gentlemen, and welcome to the ALLETE conference call announcing the first-quarter 2016 financial results. As a reminder, this conference is being recorded. I would now like to turn the call over to Mr. Al Hodnik, Chief Executive Officer. Sir, you may begin.

Al Hodnik: Thank you for joining us this morning. With me is ALLETE's Chief Financial Officer, Steve DeVinck. This morning we reported our first-quarter financial results that delivered earnings-per-share of $0.93 on revenue that was up almost 6% over last year.

I am pleased with our financial performance for the quarter and believe ALLETE is well positioned to deliver sustainable value to our shareholders. These financial results demonstrate the synergies of ALLETE's businesses in challenging times and the strength of our strategic direction.

We started this year facing headwinds similar to those in 2015, the most notable coming from a decline in power demand for Minnesota Power's taconite customers. Our regulated businesses continue to manage cost, as they have always done getting through these down cycles, without compromising customer service or reliability.

Additionally, our emerging and complementary energy infrastructure and related services companies posted financial results in line with our expectations. And we expect further growth as they execute against their strategies.

ALLETE Clean Energy and U.S. Water Services' strategies are designed to capitalize on the country's desire for cleaner energy sources and conservation. This to meet changing societal expectations, regulation and resource scarcity.

Additions of new wind generation facilities in Southern Minnesota and Pennsylvania last year significantly contributed to strong financial performance at ALLETE Clean Energy. ACE currently owns and operates about 537 megawatts of fully contracted wind generating capability and is well positioned to meet the nation's call for more renewable energy.

We remain excited about the prospects for U.S. Water Services, our newest member to the ALLETE family of businesses. U.S. Water experienced impressive revenue growth in the first quarter. Earnings for the Company reflect results from selling certain products which are seasonal in nature with higher demand typically realized in warmer months.

Attention to the water and energy nexus continues to increase and we believe changing regulation and societal expectations will drive growth and improved profitability for this business. Similar to ALLETE Clean Energy, U.S. Water will further balance and complement our core regulated businesses while providing long-term earnings growth.

We are seeing encouraging signs relative to the steel dumping that has negatively impacted taconite production on Minnesota's iron range. The United States Department of Commerce has made preliminary affirmative determinations in its duty and anti-dumping investigations. Final determinations are expected in 2016.

According to the U.S. Census Bureau, February 2016 year-to-date imports for consumption of steel products are down approximately 40% compared to February of 2015. Consequently, we are pleased that the import share of the domestic market has fallen from a peak of 34% in March of last year to roughly 24% of this year.

Auto production in the United States remains very strong. All of this a reminder that there is no lack of domestic steel demand. In addition, Cliffs Natural Resources recently reported stronger than anticipated Q1 financial results and affirmed that it will be restarting its previously idled Northshore mine in May of this year.

Cliff's CEO, Lourenco Goncalves, announced on the recent earnings call that they fully expect United Taconite to restart later this year. While Northshore Mining is not a large power customer of Minnesota Power, we are nonetheless pleased with these developments.

Given nominations as we know them, however, in the near term, we believe our full-year earnings will likely be in the lower half of our earnings guidance range of $3.10 to $3.40 per share. Again, this expectation reflects our current view of industrial sales at Minnesota Power.

The midpoint of our original earnings guidance reflected production levels of Minnesota Power's taconite customers of approximately 35 million tons in 2016. We now estimate 2016 taconite production to be between 30 million and 32 million tons.

We are preparing for our next general rate case at Minnesota Power and will be able to file later this year. Some factors affecting rate case timing decisions include current depreciation dockets and approval of our Integrated Resource Plan currently before regulators and the outlook for industrial sales.

We expect to have more specific information when we release second-quarter financial results. We remain committed to maintaining reasonable and competitive rates for our customers while providing a fair rate of return to our investors.

I am pleased with ALLETE's financial results for the quarter and am confident in our ability to deliver sustainable shareholder value. I will make some additional comments after Steve takes you through the quarterly financial results. Steve?

Steve DeVinck: Thanks, Al. And good morning, everyone. Before I begin I encourage you to refer to the 10-Q we filed earlier today for more details on the quarter.

For the first quarter of 2016 ALLETE reported earnings of $0.93 per share on net income of $45.9 million and operating revenue of $333.8 million. This compares with $0.85 per share on net income of $39.9 million and operating revenue of $320 million in 2015.

Earnings in 2015 included $3 million or $0.06 per share of acquisition costs related to our acquisition of U.S. Water Services in February of last year.

Earnings from ALLETE's regulated operations segment, which includes Minnesota Power, Superior Water, Light and Power and our investment in the American Transmission Company were $42.4 million compared with $41 million in 2015.

This year's results reflect higher cost recovery rider revenue and lower operating and maintenance expenses, mostly offset by a decrease in kilowatt hour sales and higher depreciation and property tax expenses.

Our equity earnings in ATC increased $600,000 after tax due to period-over-period changes in ATC's estimate of a refund liability related to MISO return on equity complaints.

Operating revenue from the regulated operations segment decreased $10.5 million or 4% from 2015 primarily due to lower kilowatt hour sales, fuel adjustment clause recoveries and gas sales partially offset by higher cost recovery rider revenue and FERC formula based rates.

Revenue decreased $8.1 million due to a 5% decrease in kilowatt hour sales. Sales to our residential, commercial and municipal customers were lower due to warmer average temperatures this year. Heating degree days were approximately 8% lower in 2016.

Sales to our industrial customers decreased 18% primarily due to reduced taconite production in 2016. Sales to other power suppliers increased 27%

mostly due to more energy available for sale resulting primarily from the reduced demand from our taconite customers.

Fuel clause recoveries decreased $5.5 million due to lower fuel and purchased power cost attributable to our retail and municipal customers. Revenue from gas sales at Superior Water, Light and Power decreased $1.8 million as a result of warmer temperatures in 2016.

Cost recovery rider revenue increased $4.7 million primarily due to the completion of our Boswell Unit 4 environmental upgrade. Revenue from our wholesale FERC regulated customers increased $1.7 million primarily due to additional environmental upgrades and other investments.

On the expense side, fuel and purchased power expense decreased $9.1 million or 11% from 2015 primarily due to lower purchased power prices and kilowatt hour sales this year compared to last year. Transmission services expense increased $1.9 million for the quarter or 13% primarily due to higher MISO related expenses.

Cost of sales decreased $1.5 million or 33% from last year due to the previously mentioned lower gas sales at Superior Water, Light and Power. Operating and maintenance expense decreased $8.1 million or 14% primarily due to a sales tax refund received this year and lower salary and benefit expenses.

In addition, conservation improvement program expenditures were less than the first quarter of 2015. Conservation improvement program expenses are recovered from certain retail customers resulting in a corresponding reduction in revenue.

We remain committed to cost containment at Minnesota Power to reduce rate increases for customers, improve our return on equity over time and mitigate some of the impacts of cyclicality facing our customers in taconite mining.

Our 2016 earnings guidance reflected lower operating and maintenance expense due to cost control initiatives with the expectation that 2016 amounts would be 5% to 10% lower than 2014 actual amounts. We are on track to meet those expectations.

Depreciation and amortization expense increased $6.2 million or 19% from 2015 primarily due to additional property plant and equipment and service. Equity earnings at ATC increased $900,000 or 23% from last year due mostly to period-over-period changes in ATC's estimate of a refund liability related to MISO return on equity complaints.

Net income at ALLETE Clean Energy increased $3.6 million and revenue increased $11.2 million over last year primarily due to wind energy facilities acquired in April and July of last year.

U.S. Water, acquired in February of last year, is a leader in integrated water management to a growing number of industrial and commercial customers throughout the United States. Revenue at U.S. Water Services increased $16.9 million compared to the period from February 10, 2015 to March 31, 2015.

The net loss at U.S. Water was in line with expectations and was $400,000 higher than the first quarter of 2015, which did not reflect a full quarter. The Company sells certain products which are seasonal in nature with higher demand typically realized after the first quarter.

The first quarter net loss also included $300,000 of after-tax expense related to purchase accounting for inventories and sales backlog. As we have discussed in previous quarters, this purchase accounting adjustment has now been fully recognized.

The Corporate and Other segment, which includes results from BNI Energy, ALLETE Properties and other miscellaneous corporate income and expenses reported a $2.1 million net loss this quarter compared to a net loss of $3.5 million for the same quarter in 2015. Earnings in 2015 included the $3 million or $0.06 per share of acquisition costs related to the acquisition of U.S. Water Services.

ALLETE's effective tax rate in the first quarter of this year was approximately 17% compared to about 13% in 2015. We anticipate the effective tax rate for

2016 will be approximately 17%, this could vary slightly if earnings expectations change.

ALLETE's financial position continues to be solid, cash from operating activities increased $21.4 million for the quarter driven primarily by higher net income and non-cash expense. Our debt to capital ratio at quarter end was 46%. Al?

Al Hodnik: Thank you for the financial update, Steve. I have a few more comments to make before Steve and I take your questions.

Regarding Minnesota Power's Energy*Forward* initiatives, we recently shared good news on Minnesota Power's proposed Great Northern Transmission Line. This proposed 220 mile 500 KV line will deliver hydro-generated electricity from Manitoba to Minnesota Power.

In an order dated April 11, 2016, the Minnesota Public Utilities Commission approved the route permit which largely follows Minnesota Power's preferred route including the international border crossing. The project has garnered considerable support, any final decision on the presidential permit by the United States Department of Energy is expected in the second quarter of 2016.

Minnesota Power expects to begin construction on the transmission line in 2017, and this project will provide investment and growth opportunities through the end of the decade.

With respect to a natural gas generation addition, Minnesota Power continues to advance the need within its resource plan currently before regulators and with other strategic partners who share a similar interest.

I would like to remind everyone that these initiatives are the latest step in how Minnesota Power is advancing its Energy*Forward* strategy and the balancing of its energy supply towards one-third renewable, one-third natural gas and one-third coal by the early 2020s.

Regarding new industrial load in our region, I have constructive news for PolyMet's proposed copper, nickel and precious metal mining operation in

Northeast Minnesota. The Minnesota Department of Natural Resources issued its record of decision on March 3 of this year finding the final EIF adequate.

The time to appeal that adequate -- EIF adequacy determination has expired and on April 19 the Department of Natural Resources initiated their required pre-application public information hearing near the mine site.

With this required step complete, formal submission of permanent applications by PolyMet can now occur. Once records of decision by the federal and state agencies on the necessary permits are received, PolyMet could move forward with its plans to construct and operate the mine.

Minnesota Power could begin to supply between 45 and 50 megawatts of new load through a 10-year power supply contract that would begin upon startup of the mining operations.

Essar is again in the midst of seeking financing to complete their Minnesota project. As you will recall, the Essar facility will result in approximately 110 megawatts of new load in Minnesota Power's wholesale municipal segment once it reaches full production levels and by taking service from the city of Nashwauk.

Given the quality of the ore body and the $1 billion plus investment made to date, we maintain a view that it is not a matter of if, but when the Essar project moves to commercial operations.

Further, just last week Cliffs Natural Resources publicly shared a view that the Essar site is favorable for a direct reduced iron facility which is an enhanced product suitable for use in electric arc furnaces.

Regarding our complementary energy infrastructure and related services businesses, ALLETE Clean Energy is positioned for earnings growth in 2016 as a result of the wind energy facilities it acquired during 2015. Opportunities within the renewable space remain very strong and ACE will continue to target acquisitions of existing facilities which have long-term power sales agreements in place.

U.S. Water Services will further complement our core regulated operations, balance our exposure to business cycles and changing demand and provide earnings growth over the long term. The Company will continue to look for strategic tuck in acquisitions which expand its geographic reach, add new technology or deepen its capabilities to serve its expanding customer base.

All of us at ALLETE are excited about our prospects and the opportunities to create shareholder value. Thank you for your continued confidence and your investment with us. At this time I will ask the operator to open up the line for your questions.

Operator: (Operator Instructions). Paul Ridzon, KeyBanc.

Paul Ridzon: What is the status of -- you had talked about special rates for energy intensive customers. Is that still a viable option?

Al Hodnik: It still is. The Minnesota Public Utilities Commission took up the docket initially here in the first quarter of the year and ultimately determined that they did not have enough information. They, in utility power lots rejected it without sort of discrimination against it in that sense.

So we are positioned right now and working with our customers to resubmit the EITE, as it is known here in Minnesota, to our regulators. And would hope to get that to the regulators again sometime in the early spring or mid spring here as we go off into the summer.

Paul Ridzon: And, Al, I think I heard you say you will be filing a rate case this year, is that correct?

Al Hodnik: We will be able to file a rate case later this year, yes.

Paul Ridzon: And how does that tie in with the energy intensive customers? Are those just -- be two separate processes?

Al Hodnik: Well, the EITE was a piece of special legislation that was passed by the Minnesota legislature of course and signed by Governor Dayton into law to help paper customers and taconite customers with their competitive challenges that they are facing.

And so, that has its own docket, if you will, or its own pathway with the regulators. It could ultimately get part of the conversation inside of a rate case because, after all, it is a rate design question. But the EITE is on its pathway and it is collateral to or connected to any rate case that we might file later this year.

Paul Ridzon: So, you are still not committing to file a rate case, you are still prepared to file one if need be?

Al Hodnik: We are prepared -- we are going to be able and ready to file a rate case. And as we said, timing around that really is stemming from sort of more clarity on filings that we have before our regulators in the moment.

We have depreciation filings before our regulators right now that are very important to the Company. Of course we have our Integrated Resource Plan before the commission at this point in time, we expect to hear on that shortly.

And then as I say, we have this industrial load growth and demand situation here in the region that we continue to manage, Paul. So we are going to be able and ready to file a rate case in the fall if we need to. We will have more clarity on that after our second-quarter earnings call.

Paul Ridzon: Understood. Thanks for clearing that up. What was your previous expectation for tonnage of taconite?

Steve DeVinck: Our original guidance, Paul, this is Steve, good morning. Our original guidance, the midpoint had approximately 35 million tons.

Paul Ridzon: OK, thank you very much.

Operator: Brian Russo, Ladenburg Thalmann.

Brian Russo: How does the 30 million to 35 million tons of taconite production assumption, how does that correlate with the percent nominations, which I believe are set at 80% for the next few months?

Steve DeVinck: So, our updated information this morning where we expect taconite production to be in the 30 million to 32 million ton range would generally correlate with that 80% of total production number that you have seen from us here the last quarter or two.

Brian Russo: So then what has changed? Because I believe the last time you reaffirmed your guidance we were at 80% as well? Is it just fine-tuning the sensitivity?

Steve DeVinck: Well, the last time we talked that 80% was for the first four months of the year. We have a better insight into the remaining eight months of the year or an insight or expectation as to what that may be.

So with that insight into the later -- the last eight months of the year we now think taconite production will be reduced from 35 million tons, that original expectation, to 30 million tons to 32 million tons.

Brian Russo: OK, got it. And just, is there any update on the Boswell depreciation study, when might we expect an outcome?

Steve DeVinck: As you know, in conjunction with Minnesota Power's Energy*Forward* plan and the related extensive environmental upgrades completed at our Boswell generating facility, we filed for depreciation use of life extensions earlier this year.

The requested useful life extension would decrease annual depreciation expense by approximately $20 million and have rate increase mitigating effects for our customers both immediate and longer-term. We have proposed to provide immediate customer benefit for approximately one-third of the annual expense reduction through our environmental cost recovery rider.

The remainder will help mitigate future rate increase needs. The Minnesota Department of Commerce requested and was granted a postponement of the proceeding until August.

Brian Russo: And did they give a reason why?

Steve DeVinck: No, we are not certain, but we think it just might be the status of other workload initiatives in front of them.

Brian Russo: OK, great. And has there been any change to the property net book value relative to your 10-K?

Steve DeVinck: No.

Brian Russo: OK, and then lastly, could you elaborate a little bit more on the ALLETE Clean Energy project pipeline?

Al Hodnik: Well, this is Al, Brian. The pipeline remains strong both on the wind and solar side as existing assets are positioned for sale or develop -- original developers want to move on. So I am not going to get specific this morning about projects that we are looking at or locations that we are looking at.

But I would say again that the pipeline remains very, very strong both on the solar and on the wind side, that ACE has plenty of opportunities before it and right now the team over there is parsing the opportunities as they have in the past and fully expect to have more opportunities later this year for us to assess at the ALLETE corporate level and potentially make investment in.

Brian Russo: OK, great. Thank you.

Operator: Chris Ellinghaus, Williams Capital.

Chris Ellinghaus: A couple of questions. Have you got any update on activity with ALLETE Properties?

Steve DeVinck: No, nothing really new to report. We continue to see about the same level of activity that we saw in 2015. So we will see how the year progresses.

Chris Ellinghaus: OK. And given the acquisition costs that were in Corporate and Other in the first quarter last year, it looks like there was a material decline in adjusted earnings, can you give us some color on that?

Steve DeVinck: So the acquisition costs were about $0.06 per share. Our earnings per share this year were $0.93 versus $0.85 last year. So if we are adjusted for that $0.06 I guess it would be $0.93 versus $0.91 last year.

Chris Ellinghaus: No, I meant just in the Corporate and Other segment. If you take out the $3 million from last year's first quarter, it would have been a loss of more like $500,000. So there was some significant decline there versus last year adjusted. So maybe $2.1 million versus minus $500,000 last year, what was the Delta there?

Steve DeVinck: Yes, I see. So you are correct. The acquisition cost of $3 million were in there last year. This year we have just more general corporate interest and taxes. So we have higher interest expense of right around $0.5 million, we also -- I am going to get in the weeds here a little bit.

But if you look at some of our disclosures, we have a contingent purchase obligation for U.S. Water that is discounted and then accreted over time through 2019 when that buyout happens. So there is accretion expense of about $600,000 related to that that is more than last year. And we have some period-to-period income tax allocations of probably another $0.5 million or so. So it is miscellaneous things like that.

Chris Ellinghaus: OK, great. And as far as the guidance on taconite production, can we infer that a significant portion of your decline and expectations is just related to the timing of United Tac coming back?

Steve DeVinck: Yes.

Chris Ellinghaus: OK, great, thanks for the color.

Operator: Sarah Akers, Wells Fargo.

Sarah Akers: With the latest news on PolyMet and Essar, can you update us on the current expectations for the in-service dates there?

Al Hodnik: Well, it is a little difficult with both to do that I guess, Sarah. The PolyMet process we are very encouraged about at the moment, the fact that the EIS adequacy determination and decision by the agencies was not litigated in any way is very good news for PolyMet. It is somewhat unprecedented too in terms of mining in Minnesota at least with regards to that.

The permit processes themselves have a bit more of a defined timeline both from the federal government side and also the state. So unlike the EIS, which had a much more sort of expansive process, if you will and an undefined timeline the permit processes are tighter. Of course there is financing that the Company needs to obtain as well.

And so, I don't know that I can give you anything more than what PolyMet has expressed already that they would hope to be moving forward to permitting in the later part of 2016 here and into 2017.

And then hopefully with construction and timing of finance and all the rest would be operating sometime in 2018 would be kind of I would think their commentary or what I see basically on their webpage with respect to their latest observation.

Essar of course is about $1 billion plus done and Essar continues to try to work on its financing, if you will, to put the rest of the project together. We are certainly not expecting any production from Essar in the kind of early 2017 timeframe as they put their financing together and as construction has played out up there. So that is the best I can offer with respect to PolyMet and Essar.

Sarah Akers: Got it, thank you. And then on the upcoming rate filing, should we expect a multi-year rate plan with step ups in years two and three or will this just be a one-year filing?

Steve DeVinck: So we are working through that right now. I have nothing really to announce on the specifics here today. As Al mentioned, when we announce second-quarter results we will have more specifics on the timing amount and some of the other factors in a rate case. So we are still working through that.

Sarah Akers: Got it. And then one more. Can you just remind us of ALLETE's deferred tax position and whether you are a cash tax payer now? And if not, how many years you expect to be a non-cash taxpayer with bonus and renewable credits?

Steve DeVinck: Yes. So, we are not a cash taxpayer right now because of all the factors you just indicated. I believe our current projections are that we will run through those net operating loss carry forwards in 2018 or 2019.

Sarah Akers: Great, thank you.

Operator: Joe Zhou, Avon Capital.

Joe Zhou: So, I just want to make sure my model is correct is that -- so now the taconite production is reduced to 30 million to 32 million tons for the year. So is that still the rule of thumb that still $0.03 per million tons for taconite production on your (multiple speakers)?

Steve DeVinck: Yes, that rule of thumb generally still holds.

Joe Zhou: OK, so you original guidance was like $3.10 to $3.40 and with -- and your original taconite production was 35 million and now it is reduced to a midpoint of 31 million. So there is 3 million tons. So that should reduce your original guidance by roughly $0.12.

So, the (inaudible) should be like roughly $2.98 to $3.28, so that is my calculation. And now you say that the earning will be in the bottom half of the guidance, so the $3.10 to $3.25. So I assume that the lower end lift by $0.10, is that because of the rate case?

Steve DeVinck: No, I don't think your math is quite accurate. So, our original guidance contemplated the midpoint contemplated taconite production of approximately 35 million tons. So the midpoint would have been $3.25.

Joe Zhou: OK.

Steve DeVinck: So that was the midpoint. So now we are expecting taconite production to be $0.30 to $0.32. So you've got to subtract that delta from that midpoint.

Joe Zhou: OK, okay.

Steve DeVinck: And that is how we get in the lower half.

Joe Zhou: It is not a leaner relationship, I cannot do that back of envelope calculation I guess. OK. So, on the timing for the rate case, can you remind us? You said that you will be able to file later this year. Are you talking about second half of this year or like toward the end of the year?

Steve DeVinck: We don't have the specific month yet that we are ready to disclose at this time. Some of the factors affecting rate case timing include decisions on our open depreciation docket, approval of our Integrated Resource Plan which is expected in June, and really the outlook for industrial sales. But we do expect to have more specific information when we release second-quarter financial results.

Joe Zhou: OK, great. Thank you very much.

Operator: Brian Russo, Ladenburg Thalmann.

Brian Russo: Just curious, are you able to file for interim rates in Minnesota rate cases?

Steve DeVinck: Brian, yes. So the way it works in Minnesota is once the filing is deemed complete, 60 days later interim rates would go into effect, of course subject to refund.

Brian Russo: OK. So they automatically go into effect, it is not like you have to request interim rates?

Steve DeVinck: We will certainly request and they will automatically go into effect.

Brian Russo: OK, got it. And then just within the guidance range, albeit at the lower end of the range, is there any assumption made on the outcome of the Boswell extension life study?

Steve DeVinck: No, we are assuming nothing for that.

Brian Russo: OK, great. Thank you very much.

Operator: Thank you. And I am showing no further questions at this time. I would now like to turn the call back to Mr. Al Hodnik for closing remarks.

Al Hodnik: Well, Steve and I thank you again for being with us this morning and we certainly thank you for your investment and interest in ALLETE. We hope to see some or all of you on our travels throughout the summer. Thank you very much.

Steve DeVinck: Thank you.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program and you may all disconnect.

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