

**EXHIBIT NO. \_\_\_(BAV-5)**  
**DOCKET NO. UE-06 \_\_\_/UG-06 \_\_\_**  
**2006 PSE GENERAL RATE CASE**  
**WITNESS: BERTRAND A. VALDMAN**

**BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND  
TRANSPORTATION COMMISSION,**

**Complainant,**

**v.**

**PUGET SOUND ENERGY, INC.,**

**Respondent.**

**Docket No. UE-06 \_\_\_**  
**Docket No. UG-06 \_\_\_**

**FOURTH EXHIBIT (NONCONFIDENTIAL) TO THE  
PREFILED DIRECT TESTIMONY OF  
BERTRAND A. VALDMAN  
ON BEHALF OF PUGET SOUND ENERGY, INC.**

**FEBRUARY 15, 2006**

**▲ McAdams ▲ Wright ▲ Ragen ▲**  
I N C O R P O R A T E D

01.25.2005

**RESEARCH**

Paul C. Latta, CFA > platta@mwrinc.com > 206.664.8897

**Puget Energy, Inc. (PSD) | \$23.70**

**Target Price: \$27.00 | BUY**

**FUNDAMENTAL SNAPSHOT**

52 Week High	\$24.81
52 Week Low	\$20.51
Shares Out (Mil)	99.7
Market Cap (Bil)	\$2.4

**EARNINGS ESTIMATES**

EPS	FY03A	FY04E	FY05E
FY	\$1.26	\$1.53	\$1.78

**IMPLIED P/E RATIOS**

P/E	FY03A	FY04E	FY05E
FY	18.8x	15.5x	13.3x

**Short Interest Up, Snow Pack Down**

- We were a little surprised to see PSD's short interest rise to 2.9 million shares this month from 1.2 million shares last month. The increase was the 12th largest monthly increase on the NYSE. With a daily average trading volume of 240,730 shares, the short interest ratio now amounts to 12.2 days to cover. We spoke with the Company to verify that there was no equity or equity derivative placement or retirement that would require shorting the stock in order to hedge. Note that another Pacific Northwest utility, IDACORP, made the list this month with the 14th largest monthly increase on the NYSE. However, IDACORP's increase was likely associated with its December secondary stock offering.
- In Puget's case, the short interest appears related to the general rate case which is nearing its scheduled March 5<sup>th</sup> conclusion. A similar step-up in short interest occurred last year with the conclusion of the power only rate case; the short interest ratio peaked at 15 days in April 2004. In general, we believe that the final resolution of the rate case will be a minor negative for PSD, and may result in a modest reduction in earnings estimates for 2005 and 2006. Note that with the current 12.2 day short position, a positive rate case resolution, while unlikely, could result in a short squeeze.
- Separately, in response to a number of local investor questions, we inquired about the implications for PSD of a very low snowpack this year (despite reasonable precipitation levels). The Company noted that there is a cap on the power cost tracker, which should limit possible negative impact here. Of course, temperatures will still be meaningful.
- **Puget Energy, Inc. is rated Buy. Our EPS estimates: FY04 \$1.53, FY05 \$1.78. Target Price: \$27.**

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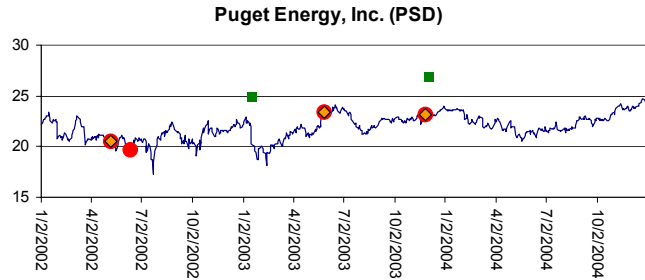
- *I, Paul C. Latta, hereby certify (1) that the views in this research note accurately reflect my personal views about any or all of the subject securities or issuers referred to in this note and (2) no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views in this note.*

**Additional required disclosures under NASD Rule 2711 are provided on the last page of this report.**

**Additional required disclosures under NASD Rule 2711 are provided on page two of this document.**

**Required Disclosures:**

	From	To	Date	Price
■	Price Target	\$25 to \$27	12/1/2003	\$23.48
◆	Added to Focus List		11/26/2003	\$23.21
●	Hold to	Buy	11/26/2003	\$23.21
◆	Removed from Focus List		5/28/2003	\$23.40
●	Buy to	Hold	5/28/2003	\$23.40
■	Price Target	To \$25	1/16/2003	\$20.24
●	Rating System Change	Buy	6/11/2002	\$19.64
◆	Added to Focus List		5/6/2002	\$20.57
●	Hold to	Buy	5/6/2002	\$20.57



● Ratings Change ◆ Focus List Change ■ Target Price Change

Price targets are subject to change as new information becomes available, and reflect our current judgment regarding this security. Note that there are risks that may impede the achievement of a predicted price target. Price targets are based on fundamental factors such as historical and projected earnings, cash flow, discounted cash flow, relative book value, peer group evaluation, relative sector valuations, and expectations on general market and economic conditions.

McAdams Wright Ragen employs a Ratings System (in effect since 6/12/2002), defined as follows.

Buy/Addition to InStock Recommended List: We expect the Stock to Outperform the Market.

Hold/Addition to InStock Recommended List: We expect the Stock to be a Market Performer.

Sell/Removal from InStock Recommended List: We expect the Stock to Underperform the Market.

Ratings System in effect between 2/7/2002 and 6/12/2002: Strong Buy, Buy, Hold, Underperform, Sell.

Ratings System in effect prior to 2/7/2002: Buy, Moderate Buy, Hold, Underperform, Sell.

	Percentage of Rated Stocks Currently Assigned this Rating	Percentage of Rated Stocks with this Rating with which MWR has had an Investment Banking Relationship in the last 12 months
Buy	50%	9%
Hold	36%	4%
Sell	14%	0%

For Price Chart and Ratings History disclosures, please go to <http://www.mwrinc.com/ClientAccess/quotesresearch.html>, or to request information, please contact Sara E. Hasan, Research Assistant, (206) 664-8854, [mwr@mwrinc.com](mailto:mwr@mwrinc.com)

This is not a complete analysis of every material fact regarding any company, industry or security. The opinions expressed here reflect our judgment at this date and are subject to change. The information has been obtained from sources we consider reliable, but we cannot guarantee the accuracy. Our firm, or its officers, research personnel, other employees or customers may have long or short positions in the securities or options of the recommended issuers, may buy and sell the securities or options, may serve as an officer or director of any company mentioned, prior to or at the time of publication of the report or thereafter.

**Additional required disclosures under NASD Rule 2711 are provided on page two of this document.**

February 3, 2005

**PUGET ENERGY, INC.**

PSD – NYSE

**Rating:****NEUTRAL****Price:** (2/3/05) \$23.90**Price Targets:**

12-18 month: \$24

5-year: \$30

**Industry:**

Utilities

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FY (Dec)	2003A	2004E*	Y-O-Y Growth	2005E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,421.4	\$2,584.8	7%	\$2,768.8	7%
Previous	-	NC		NC	
Price/Revenue ratio	.9x	.9x		.9x	
<b>EPS Revised</b>	<b>\$1.22</b>	<b>\$1.25</b>	2%	<b>\$1.60</b>	28%
Previous	-	NC		NC	
Price/EPS ratio	19.6x	19.1x		15.0x	
<b>EBITDA (\$M)</b>	\$616.0	\$625.9	2%	\$699.2	12%
EV/EBITDA ratio	8.1x	7.9x		7.1x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/04A	<b>\$0.67</b>	-	\$743.5	-	\$208.7
6/30/04A*	<b>(\$0.07)</b>	-	\$515.9	-	\$95.0
9/30/04A*	<b>\$0.11</b>	-	\$515.0	-	\$124.9
12/31/04E*	<b>\$0.54</b>	NC	\$810.5	NC	\$197.3

\*See detail of footnote on page 2.

**Valuation Data**

Long-term growth rate (E)	5%
Total Debt/Cap (9/30/04)	61.2%
Cash per share (9/30/04)	\$0.25
Book value per share (9/30/04)	\$16.67
Dividend (yield)	\$1.00 (4.2%)
Return on Equity (T-T-M)	7%

**Trading Data**

Shares outstanding (M)	99.7
Market Capitalization (\$M)	\$2,382
52-week range	\$20.51 - \$24.81
Average daily volume (3 mos.) (K)	290
Float	100%
Index Membership	S&P 400 MidCap

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. It is also developing a non-regulated utility services business called InfrastruX.

**Earnings Preview. Initiating 2006 EPS Forecast.**

- Puget Energy expects to report 4Q'04 financial results after the close of the stock market on Wednesday, February 9, 2005. Management has also scheduled a conference call to discuss results on Thursday, February 10, at 7:00 a.m. PST
- We are forecasting 4Q'04 EPS of \$0.54 compared to \$0.44 in 4Q'03. We believe results will be held back by warmer than normal temperatures. Heating-degree days from October 1, 2004 through December 31, 2004 in the company's service territory were 6% warmer than normal and 3% warmer than a year earlier.
- We are maintaining our 2005 EPS estimate of \$1.60 based on an assumption of normal weather and a \$70 million annualized increase in electric and gas rates in Washington starting on or about March 1. (The company has requested a \$149.5 million increase in rates.) While temperatures in January started off cold, a mid-January thaw sent temperatures higher, and temperatures for the entire month averaged 7% warmer than normal and 8% warmer than year ago.
- We are initiating a 2006 EPS forecast of \$1.76 based on an assumption of normal weather and the carry-over benefits of the assumed 2005 rate increase in Washington.
- We are maintaining our 12-18 month target price of \$24, or 14.3x the average of our 2005 and 2006 EPS estimates. Over the past decade, the stock of PSD has traded at a median 14.7x multiple of year-forward earnings. With the share price near this target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.2%.

Please refer to pages 5-6 of this report for detailed disclosure and certification information.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*Includes a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04.

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

	2000	2001	2002	2003	9/30/2004
<b>Assets</b>					
<b>Utility Plant:</b>					
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,361,504
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,845,141
Common plant	351,051	362,670	378,844	390,622	406,395
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,424,162)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,188,878
<b>Other Property and Investments:</b>					
Investment in Bonneville Exchange Power Contract	58,189	54,663	51,136	47,609	44,964
Goodwill, net	45,655	102,151	125,555	133,302	133,069
Intangibles, net		16,059	18,652	18,707	17,239
Non-utility property and equipment, net		48,369	80,855	91,932	95,024
	188,453	96,007	101,932	110,543	108,703
Total other property and investments	292,297	317,249	378,130	402,093	398,999
<b>Current Assets:</b>					
Cash	36,383	92,356	176,669	27,481	21,211
Restricted cash			18,871	2,537	3,777
Accounts receivable, net					
Less: Allowance for doubtful accounts					
Total accounts receivable	343,108	279,321	279,623	227,115	202,423
Unbilled revenues	211,784	147,008	112,115	131,798	75,928
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	117,081
Purchased gas receivable	96,050	37,228			18,172
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	33,386
Taxes receivable					
Prepayments and other	11,607	11,277	11,323	12,200	23,360
Total current assets	797,933	660,838	672,744	493,852	495,338
<b>Long-Term Assets:</b>					
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	135,662
PURPA buyout costs	243,071	244,635	243,584	227,753	215,369
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	25,076
Power cost adjustment mechanism				3,605	
Other	177,609	239,941	269,876	315,739	386,090
Total Long-term assets	628,030	680,909	690,388	698,513	762,197
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,845,412</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>					
Common stock	\$859,038	\$870	\$936	\$991	\$997
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,617,164
Earnings reinvested in the business	92,673	32,229	36,396	58,217	54,462
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(11,348)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,661,275
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,218,042
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,161,456
Minority interest in equity of a consolidated subsidiary			10,629	11,689	12,121
<b>Current Liabilities:</b>					
Accounts payable	410,619	167,426	205,619	214,357	165,052
Short-term debt	378,316	348,577	47,295	13,893	24,511
Current maturities of long-term debt	19,000	119,523	73,206	246,829	90,305
Purchased gas liability	0	0	83,811	11,984	
Accrued expenses:					
Taxes	103,996	70,708	62,562	77,451	26,568
Salaries and wages	17,445	14,746	11,441	12,712	12,594
Interest	43,955	42,505	37,942	32,954	41,018
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	4,270
Tenaska disallowance reserve					11,212
Other	26,685	46,178	47,761	46,378	46,498
Total current liabilities	1,000,016	844,808	572,047	660,194	422,028
Deferred Income Taxes	608,185	605,315	730,675	755,235	808,991
Other Deferred Credits	132,869	196,339	267,458	340,893	440,816
Commitments and Contingencies	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	0
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,845,412</b>

## PUGET SOUND ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)	4Q03	2003	1Q04	2Q04	3Q04	4Q04E	2004E	1Q05E	2Q05E	3Q05E	4Q05E	2005E	2006E
OPERATING REVENUES:													
Electric	\$389,800	\$1,439,358	\$392,495	\$303,091	\$322,669	\$416,572	\$1,434,827	\$407,946	\$320,446	\$340,097	\$439,012	\$1,507,501	\$1,586,424
Gas	251,524	634,230	275,692	119,479	89,432	298,884	783,487	314,038	130,949	97,335	334,007	876,329	915,741
Other	89,815	347,830	75,283	93,369	102,850	95,000	366,502	80,850	96,250	107,800	100,100	385,000	400,000
Total operating revenues	731,139	2,421,418	743,470	515,939	514,951	810,456	2,584,816	802,834	547,646	545,232	873,119	2,768,830	2,902,166
OPERATING EXPENSES:													
Energy costs:													
Purchased electricity	205,217	753,084	196,367	173,847	147,589	223,638	741,441	208,052	147,405	163,927	237,067	756,451	793,212
Purchased gas	147,337	327,132	162,407	63,703	44,574	192,903	463,587	194,827	72,356	51,246	214,503	532,932	571,902
Electric generation fuel	17,584	64,999	13,988	21,014	25,130	23,745	83,877	14,278	19,227	23,807	24,146	81,457	77,735
Residential Exchange	(51,289)	(173,840)	(54,423)	(35,362)	(34,014)	(51,221)	(175,020)	(54,257)	(35,570)	(34,010)	(51,364)	(175,200)	(175,000)
Unrealized (gain)/loss on derivative instruments	(278)	106	(87)	(2,849)	1,894	1,100	58	0	0	0	0	0	0
Utility operations and maintenance	78,070	289,702	73,855	73,201	67,093	76,000	290,149	75,000	78,000	69,000	78,000	300,000	306,000
Other operations and maintenance	74,900	303,972	67,002	78,545	87,361	81,000	313,908	72,000	81,000	89,000	85,000	327,000	335,000
Depreciation and amortization	60,442	236,866	60,288	61,122	62,204	62,500	246,114	61,500	64,500	63,500	64,000	253,500	258,000
Merger and related costs/conservation amort.	9,544	33,458	8,190	4,809	4,747	4,500	22,246	7,000	5,000	5,000	5,000	22,000	22,000
Taxes other than federal income taxes	60,608	208,395	67,492	45,622	46,024	62,000	221,138	69,000	47,000	47,000	64,000	227,000	235,000
Federal income taxes	36,010	72,369	38,711	(2,929)	8,524	37,204	81,510	41,875	7,674	8,749	45,608	103,906	115,100
Total operating expenses	638,145	2,116,243	633,790	480,723	461,126	713,369	2,289,008	689,275	486,592	487,219	765,959	2,429,045	2,538,948
OPERATING INCOME	92,994	305,175	109,680	35,216	53,825	97,087	295,808	113,558	61,053	58,013	107,161	339,785	363,218
OTHER INCOME	(4,050)	1,564	64	1,586	318	500	2,468	500	500	500	500	2,000	2,000
INCOME BEFORE INTEREST CHARGES	88,944	306,739	109,744	36,802	54,143	97,587	298,276	114,058	61,553	58,513	107,661	341,785	365,218
INTEREST CHARGES, net of AFUDC	45,483	183,973	43,399	43,270	42,834	43,500	173,003	43,750	45,000	45,250	45,500	179,500	184,000
Mandatorily redeemable securities interest	24	1,072	23	23	23	23	92	23	23	23	23	92	92
Minority interest	71	177	(43)	289	162	100	508	150	150	150	150	600	600
Discontinued Operations:													
NET INCOME before effect of acct. change	43,366	121,517	66,365	(6,780)	11,124	53,964	124,673	70,135	16,380	13,090	61,988	161,593	180,526
FAS-133 transition adjustment loss (net of tax)		169					0					0	
Less: Preferred stock dividends/ redemptions	372	5,151					0					0	
INCOME FOR COMMON STOCK	\$42,994	\$116,197	\$66,365	(\$6,780)	\$11,124	\$53,964	\$124,673	\$70,135	\$16,380	\$13,090	\$61,988	\$161,593	\$180,526
DILUTED COMMON SHARES OUT. --WEIGHTED	97,228	95,309	99,367	99,371	100,043	100,343	99,781	100,643	100,943	101,243	101,543	101,093	102,293
INCOME FOR COMMON STOCK													
Utility before accounting change	\$43,833	\$113,824	\$66,854	(\$9,634)	\$8,126	\$51,964	\$117,310	\$69,635	\$12,980	\$9,490	\$59,488	\$151,593	\$169,526
Cumulative effect of accounting change		169											
Non-utility	(839)	2,204	(489)	2,854	2,998	2,000	7,363	500	3,400	3,600	2,500	10,000	11,000
Total	\$42,994	\$116,197	\$66,365	(\$6,780)	\$11,124	\$53,964	\$124,673	\$70,135	\$16,380	\$13,090	\$61,988	\$161,593	\$180,526
EARNINGS PER COMMON SHARE													
Utility	\$0.45	\$1.19	\$0.67	(\$0.10)	\$0.08	\$0.52	\$1.18	\$0.69	\$0.13	\$0.09	\$0.59	\$1.50	\$1.66
Cumulative effect of accounting change		\$0.00											
Non-utility	(0.01)	0.02	(0.00)	0.03	0.03	0.02	0.07	0.00	0.03	0.04	0.02	0.10	0.11
DILUTED EARNINGS PER SHARE	\$0.44	\$1.22	\$0.67	(\$0.07)	\$0.11	\$0.54	\$1.25	\$0.70	\$0.16	\$0.13	\$0.61	\$1.60	\$1.76

\* Company adopted EITF 03-11 on Jan. 1, 2004, which requires most non-trading derivative instruments to be shown net in the income statement. For example, 1Q'03 "sales to other utilities & marketers," a subset of electric revenues, were shown originally as \$57.2 mm, and now are shown as \$21.9 mm. A similar offsetting adjustment was also made to lower purchased electric expenses, leaving net income unchanged. The company has now provided the quarterly reclassifications for the first nine months of 2003. To align our 4Q'03 data with the reclassified nine month 2003 data, we are estimating that 4Q'03 revenues of \$26.7 million will be reclassified as \$15.7 million and 4Q'03 purchased electric costs of \$216.2 million will be reclassified as \$205.2 million.

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D.A. Davidson & Co. expects to receive, or intends to seek, compensation for investment banking services from this company in the next three months.

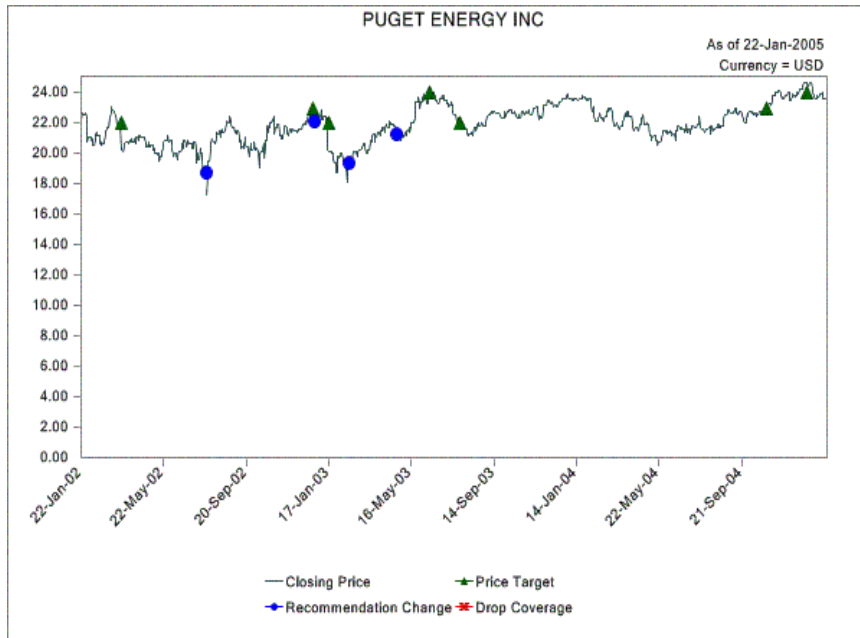
D.A. Davidson & Co. is a full service investment firm that provides both brokerage and investment banking services. James L. Bellessa, Jr., CFA, the research analyst principally responsible for the preparation of this report, will receive compensation that is based upon (among other factors) D.A. Davidson & Co.'s investment banking revenue. However, D.A. Davidson & Co.'s analysts are not directly compensated for involvement in specific investment banking transactions.

I, James L. Bellessa, Jr., CFA, attest that (i) all the views expressed in this research report accurately reflect my personal views about the common stock of the subject company, and (ii) no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

### Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 12/31/04)	Buy	Hold	Sell
Corresponding Institutional Research Rating	Buy	Neutral	Underperform
Distribution of Institutional Research Ratings	42%	45%	13%
Corresponding Retail Research Rating	Buy, Core/Buy	Hold, Core/Hold	Avoid
Distribution of Retail Research Ratings	71%	29%	0%
Distribution of combined ratings	47%	42%	11%
Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos	9%	8%	5%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
Strong Buy, Buy, Neutral, Underperform

#### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	27-Dec-2004	24.62	24.00
14-Feb-2003	19.44	BUY	25-Oct-2004	22.71	23.00
26-Dec-2002	22.10	NEUTRAL	24-Jul-2003	22.05	22.00
22-Jul-2002	18.73	BUY	12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00
			21-Mar-2002	20.29	22.00



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**US Equity Research**  
J.P. Morgan Securities Inc.  
February 10, 2005

# Puget Energy

Exiting InfrastruX, Maintain OW, but Cutting Estimates

## *Puget Energy*

**Overweight**

<i>Ticker</i>	<i>PSD</i>	<i>EPS</i>	<b>2004A</b>	<b>2005E (Old)</b>	<b>2005E (New)</b>	<b>2006E (Old)</b>	<b>2006E (New)</b>
<b>Price(02/09/05)</b>	\$24.04	<b>1Q (Mar)</b>	\$0.67				
<b>52-Wk.Range</b>	\$20.52-24.81	<b>2Q (Jun)</b>	\$0.16				
<b>Mkt.Cap(BN)</b>	\$2.39	<b>3Q (Sep)</b>	\$0.11				
<b>Fiscal Year</b>	Dec	<b>4Q (Dec)</b>	\$0.61				
<b>Shares O/S(MM)</b>	99.49	<b>FY</b>	\$1.60	\$1.75	\$1.65	\$1.85	\$1.80
		<b>P/E FY</b>	15.0	13.7	13.7	13.0	13.0

\*Official EPS estimates are rounded to the nearest \$0.05.

Puget is exiting its underperforming construction company, InfrastruX, its only non-utility business. We are cutting EPS to reflect InfrastruX as discontinued ops and some regulatory lag. A key point for the stock should occur by March 5th when the Washington regulator will rule in PSD's rate case.

- Excluding the \$0.77 per share writedown on InfrastruX, PSD reported 4Q04 EPS of \$0.61, ahead of our estimate of \$0.55 and the consensus estimate of \$0.56. Better electric margins, lower income taxes, and a writedown in 4Q03 were only partially offset by higher D&A, lower gas margins, and share dilution.
- PSD intends to sell InfrastruX sometime in 2005. On debt of \$160 million and equity of \$33 million, the enterprise value is nearly \$200 million and represents about 5.5x EBITDA, about inline with our valuation of the business. We believe the intended sale is a positive development as it would eliminate an underperforming businesses and Puget could redeploy modest cash proceeds to help fund its utility.
- On its conference call with investors, PSD noted higher D&A and O&M would impact earnings in 2005. However, PSD will attempt to recover the costs through the regulatory process. We are cutting 2005E EPS to \$1.65 from \$1.75 and 2006E EPS to \$1.80 from \$1.85 to reflect the regulatory lag as well as reclassification of \$0.05E EPS for InfrastruX to discontinued ops in 2005.
- A key decision should come for Puget by March 5th. The Washinton regulator is expected to rule on Puget's pending rate case. If the ruling is constructive (allowed ROE of about 10.25% or better and at least an actual equity layer) then we believe the long-term investment case for PSD remains viable as it will invest in its utility infrastructure. We believe anything less calls our investment case into question.
- Puget looks undervalued based on our 10-year DCF analysis. It also trades at 13.3x

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our 2006E EPS versus the group average of 14.5x. We believe that Puget's shares are undervalued because investors have not incorporated Puget's potential strong EPS outlook (if its rate case is resolved constructively) into their valuation. We are maintaining our Overweight rating.

### **EPS Estimate Change Reconciliation**

We are cutting our 2005E EPS to \$1.65 from \$1.75 and our 2006E EPS to \$1.80 from \$1.85. A broad reconciliation of our 2005E EPS change starts with our old 2005 EPS estimate of \$1.75 and adds \$0.10 for 2004 outperformance (\$1.60 actual 2004 EPS versus our estimate of \$1.50). We then subtract \$0.10 for higher D&A not recovered in 2005 due to regulatory lag and \$0.05 for higher O&M not recovered in 2005 due to regulatory lag as well as our estimated InfrastruX EPS of \$0.05, which we are excluding because it will be moved to discontinued ops in 2005. The net of these changes is \$1.65.

A broad reconciliation of our 2006E EPS change starts with our old 2006 EPS estimate of \$1.85 and adds \$0.10 for 2004 outperformance, makes the same subtractions as our 2005 estimated EPS adjustments but then adds back 50% of the regulatory lag penalty due to our expectation that the company will move to recover at least a portion of the regulatory lag impact by the middle of 2006.

We are not changing our rate case outcome assumptions; however, investors should note that the reconciliation numbers are rounded and do not tie exactly to our EPS estimates because we also round our actual estimates to the nearest \$0.05.

### **Valuation and Rating Analysis**

Puget is seeking to increase its rates by \$129 million. We project that it will be allowed to raise its rates \$56 million versus the Staff's current proposal to allow Puget to raise its rates \$29 million. We believe Puget's near-term EPS growth outlook, as well as our forecast for 10% long-term EPS growth, is not reflected in the stock's current valuation. Based on our DCF analysis, we believe Puget's shares are undervalued, and on a relative P/E basis, Puget looks undervalued as well. It is currently trading at 13.9x our 2005 EPS estimate. This represents a discount to the industry average P/E multiples for 2005E of 15.5x. Furthermore, we note that Puget pays a dividend above the industry average.

### **Risks to Our Rating**

Our investment thesis for Puget's shares is based primarily on it being allowed to increase its rates to recover investment in its utility infrastructure, improve its utility ROE, and continue to improve its balance sheet. If Puget is not allowed to increase its rates, it will continue to earn a utility ROE that is well below the industry average and will likely have difficulty further improving its balance sheet materially. In this case, our outlook for the shares would be less favorable.

### **Companies Recommended in This Report**

Puget Energy (PSD/\$24.04/Overweight)

### **Analyst Certification**

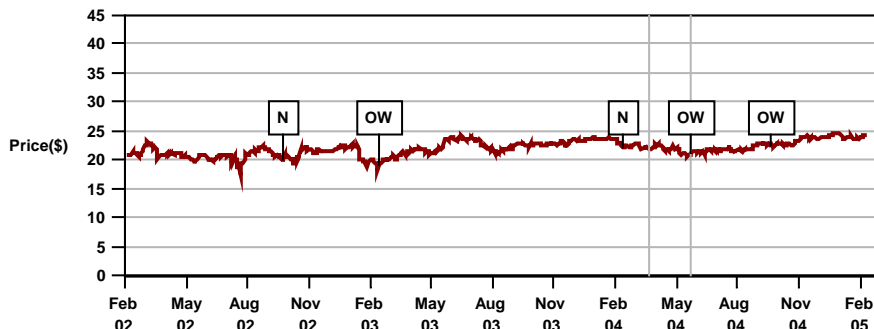
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**Puget Energy (PSD) Price Chart**



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.  
 Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.  
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JPM Global Equity Research Coverage	39%	42%	19%
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Equity Research  
North America

United States of America

Electric Utilities

# Puget Energy

Reuters: PSD.N Bloomberg: PDS NYSE: PSD

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## Change in Earnings Forecast

February 10, 2005

# Unreg Sale a Positive; Rate Case Uncertainty Remains

STOCK RATING	EQUAL-WEIGHT
Price (February 10, 2005)	\$24.00
Price Target	NA
52-Week Range	\$24.81-20.52

Stock ratings are relative to the analyst's industry (or industry team's) coverage universe.

GICS SECTOR	UTILITIES
US Strategist Weight	2.6%
S&P 500 Weight	3.1%

WHAT'S NEW	
2006e ModelWare EPS	\$1.68

WHAT'S CHANGED	
2005e ModelWare EPS	To \$1.66 to \$1.59

- **Conclusion: InfrastruX sale refocuses mgmt.; tough reg environment continues**  
Management announced on its 4Q04 call plans to monetize its InfrastruX business and refocus its attention on the utility and necessary capacity additions.
- **What's New: Slightly higher wind spend; op costs up significantly in '05**  
We had previously anticipated wind spending would be about \$1,100/KW while it now appears that it will be closer to \$1,333/KW. This adds about \$35 mm of additional spend for every 150 MW added. O&M is likely to be about \$0.05 higher and D&A about \$0.05 to \$0.10 higher in 2005.
- **Implication: Trimming '05 due to no InfrastruX and higher costs**  
InfrastruX contributed about \$0.06 to '04 results. Rate relief helps offset much of the cost increases at the utility. '06E shows some improvement as a full-year of rate relief, modest earnings from wind additions and underlying growth drive the \$0.10 of improvement.
- **Industry View: Cautious**  
Historical tendency of the electrics is to underperform in a rising interest rate environment. Relative P/E is near the top of 15-year range, which may be difficult to sustain given our view of rising capex and declining margins for many utilities over the next several years.

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FY ending Dec 31:	2003	2004e	2005e	2006e
ModelWare EPS (\$)	—	1.60	1.59	1.68
Prior EPS Ests. (\$)	—	—	1.66	—
First Call Consensus (\$)	1.26	1.52	1.68	1.81
Revenue (\$ m)	—	2,608	2,650	2,795
P/E	—	15.0	15.1	14.3
P/E Rel. to (local index) (%)	—	—	—	—
Price/Book	—	1.4	1.3	1.1
EV/EBITDA	—	7.3	7.2	6.8
Dividend Yield (%)	4.2	4.2	4.2	4.2
Market Cap (\$ m)	2,396			
Enterprise Value (\$ m)	—			
Debt/Cap (12/03)(%)	—			
Return on Equity (12/03)(%)	—			
Shares Outstanding (m)	99.7			
		Q'trly EPS estimate	2006e curr	2007e prior
		Q1	—	—
		Q2	—	—
		Q3	—	—
		Q4	—	—

e = Morgan Stanley Research estimates. Please see explanation of Morgan Stanley ModelWare initiative later in this report.

## *Unreg Sale a Positive; Rate Case Uncertainty Remains*

### Company Description

*Puget Sound Energy is a combination electric/gas utility serving the western portion of Washington state. The company delivers electricity, natural gas, and energy solutions to more than 1.2 million customers in Washington State.*

### Summary and Investment Conclusion

PSD trades at about the middle of the range for utility P/E at about 15x 2005E. The sale of its InfrastruX subsidiary, an unregulated utility infrastructure business, will not likely bring in significant cash but it may refocus management's attention on the underlying utility. PSD is making modest capacity additions of about 150 MW annually over the next few years as part of a long-term resource plan, which may offer some long-term EPS growth but near-term share issuance. The company's rate case, expected to be resolved by March 2005, is likely to be neutral to earnings as costs have also risen significantly.

### What happened

—**PSD reported 4Q04 EPS of \$0.61 before goodwill write-off of (\$0.77).** Puget Sound Energy earned \$0.59. Electric margins were up \$0.08 vs. 4Q03 while gas margin was down \$0.02 as warmer weather hurt gas sales.

—**For 2004, PSD reported EPS of \$1.60 before goodwill write-off.** InfrastruX earned \$0.06, slightly exceeding our expectation of \$0.05. Electric utility customer growth was 2.2% and gas customer growth was 4.2%. Interest expense was \$0.14 lower in 2004. The Frederickson acquisition added about \$0.02 from higher rates through the PCORC, a regulatory mechanism that allows expedited review and recovery for power costs.

### What we liked

—**Decision to monetize InfrastruX puts management's focus back on the utility.** PSD announced that it would monetize its InfrastruX subsidiary and will take a \$77 million goodwill write-down related to the business. InfrastruX currently carries about \$160 million of debt and about \$33 million of equity book value after the write-down. Though it appears that cash proceeds are likely to be modest at around book value, this creates some additional liquidity for its spending on additional capacity and may delay equity issuance. InfrastruX's better than expected 2004 results might indicate some potential improvement in the business. We believe that regulators viewed InfrastruX negatively as it was a potential drain of cash from the utility.

—**Wind capacity additions appear about on track.** The 150 MW Hopkins Ridge wind project is expected to be online by December 2005 and the 160 MW Wild Horse wind project is scheduled for 2006. Management indicated that the Wild Horse project will be completed regardless of whether or not the wind PTC is renewed for 2006. We expect equity offerings of about \$175 million in total over the next two years to finance the projects, in addition to about \$250 million in debt. This new equity will likely dampen much of the initial EPS growth associated with the new capacity.

### What gave us concern

—**Cap ex slightly higher for wind and maintenance.** PSD indicated it will spend about \$380 million in maintenance capex in 2005 and about \$200 million for the Hopkins Ridge project. We previously anticipated maintenance spending of about \$370 million and wind spending of about \$165 million. We earlier estimated that wind projects would cost about \$1,100/kW while it now appears that they cost around \$1300/kW. Although PSD is likely to recover the higher costs through its PCORC mechanism, there may still be some regulatory lag associated with maintenance and wind spending and the higher spending raises the company's funding needs.

—**Operating expenses are moving up significantly.** Management indicated that O&M would likely be about \$10 million higher in 2005 and D&A would be about \$10-20 million higher. This creates a drag of about \$0.10- \$0.15 in EPS.

### What has changed

—**Lowering 2005 EPS to \$1.59 from \$1.66 and introducing 2006 EPS of \$1.68.** Much of the decrease is due to no EPS contribution from the InfrastruX subsidiary. Rate relief, lower interest expense and underlying utility growth offset much of the rise in operating costs. Wind additions to rate base are not likely to affect results significantly in 2005 but will add a bit to 2006 EPS.

—**Rate case outcome expected to be about neutral.** PSD recently revised its rate request in a brief filed January 18 and requested an electric rate increase of \$99.8 million versus its previous request of \$81.9 million. Its gas rate increase continues to be about \$46.2 million. WUTC Staff offered a revised increase of \$15.8 million for electric and

\$11.3 million for gas, which is slightly lower overall than its previous recommended increase of \$21.3 million for electric and \$8.1 million for gas. The major disagreement is over the cost of capital as Puget is attempting to reach a 45% equity ratio and 11.75% ROE while Staff recommends a 42% equity ratio and 9% ROE.

We expect a 42% equity ratio and 10.5% ROE which implies utility EPS of about \$1.62. A decision from regulatory commissioners is due by March 5, 2005. Once the rate case is decided, PSD will issue 2005 guidance.

Exhibit 1

**Potential EPS Outcomes to General Rate Case**

	<b>PSE Request:</b>	<b>MS Target</b>	<b>Staff</b>
<b>Rate Base \$3.7 Billion</b>			
ROE:	11.75%	10.50%	9.00%
Equity Ratio:	45%	42%	42%
Earnings	196	163	140
<b>EPS</b>	<b>1.94</b>	<b>1.62</b>	<b>1.38</b>
Total Rate of Return	9.12%	8.25%	7.60%
Earnings	337	305	281
Interest	142	142	142
Adjusted Earnings	195	163	139
<b>EPS</b>	<b>1.94</b>	<b>1.62</b>	<b>1.38</b>

Source: Company data, Morgan Stanley Research



Exhibit 2

**Puget Energy Income Statement**

	2001A	2002A	2003A	2004E	2005E	2006E
Revenues	2,887	2,392	2,492	2,605	2,295	2,433
Purchased electricity	919	645	823			
Residential exchange	(76)	(150)	(174)			
Purchased gas	537	405	327			
Electric generation fuel	281	114	65			
Unrealized (gain) loss on derivative instruments		(11)	(12)	0		
Fuel & purchased power	1,650	1,002	1,042	1,082	1,068	1,093
Gross margin	1,236	1,390	1,450	1,522	1,226	1,341
Utility O&M	266	286	290			
Other O&M	157	273	304			
O&M	423	559	594	614	302	312
Other Expense				-	-	-
One time items				4		
Depreciation and amortization	218	229	237	246	243	267
Conservation amortization	6	18	33	26	26	26
D&A	224	246	270	272	269	293
Other taxes	213	215	208	222	227	256
Operating income	377	369	378	411	429	479
Equity investments				-	-	-
AFUDC-Equity				-	-	-
Other income	15	5	6	4	4	4
EBIT	391	374	383	415	433	483
EBITDA	616	621	653	687	702	777
Interest expense	195	198	188	177	174	178
AFUDC-Debt	(4)	(2)	(3)	(4)	(4)	(4)
Net Interest Expense	190	196	185	172	170	174
Pretax income	201	178	198	243	263	309
Taxes	80	59	72	90	103	121
Net Income before Min Int	122	119	126	152	160	188
Preferred Stock	8	8	5		-	-
Minority Interest	-	1	0	(7)	-	-
Recurring Net Income	113	110	120	159	160	188
Income from Discontinued Operations						
Change in Acct	(15)		(0)			
Non-recurring income			(4)	(28)	(7)	(5)
Reported net income	98	110	116	132	153	183
<b>Basic On-Going EPS</b>	<b>\$1.21</b>	<b>\$1.25</b>	<b>\$1.27</b>	<b>\$1.60</b>	<b>\$1.59</b>	<b>\$1.68</b>
<b>Diluted On-Going EPS</b>	<b>\$1.31</b>	<b>\$1.24</b>	<b>\$1.26</b>	<b>\$1.60</b>	<b>\$1.59</b>	<b>\$1.68</b>
Basic GAAP EPS	\$1.14	\$1.25	\$1.23	\$1.33	\$1.52	\$1.64
Average Basic Shares	86	88	95	99	100	112
Diluted GAAP EPS	\$1.14	\$1.24	\$1.22	\$1.32	\$1.52	\$1.63
Average Diluted Shares	87	89	95	100	101	112
Dividend per share	\$1.84	\$1.21	\$1.00	\$1.00	\$1.00	\$1.00

Source: Company data, Morgan Stanley Research

Puget Energy – February 10, 2005

**Please see analyst certification and other important disclosures starting on page 6.**



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**ModelWare is a proprietary framework for financial analysis created by Morgan Stanley Research.** This new framework rests on the principles of comparability, transparency, and flexibility, and aims to provide investors with better tools to view the anticipated performance of an enterprise. The result of an 18-month global effort, ModelWare harmonizes the underlying data and calculations in Morgan Stanley models with a broad set of consistently defined financial metrics. Our analysts have populated the database with over 2.5 million data points, based on an extensive taxonomy of more than 3,500 unique metrics and more than 400 Morgan Stanley calculations. The ModelWare framework will also have the flexibility to allow analysts and investors to quickly customize their own analytical approach.

**What makes the ModelWare architecture distinctive lies in the separation of data from calculations.** Its transparency will permit users to see every component of every calculation, to choose elements or recombine them as they wish without laborious adjustments or recalculations. When choices must be made in defining standard or industry-specific measures, ModelWare defaults to economic logic, rather than favoring one accounting rule over another. This discipline facilitates comparability across sectors and regions. Underlying the ModelWare data is a new set of systems that check the internal consistency of forecast data in each of our analyst's models.

**ModelWare EPS** illustrates the approach taken. It represents ModelWare net income divided by average fully diluted shares outstanding. ModelWare net income sums net operating profit after tax (NOPAT), net financial income or expense (NFE), and other income or expense. ModelWare adjusts reported net income to improve comparability across companies, sectors, and regions. These adjustments include the following: We exclude goodwill amortization and items deemed by analysts to be "one-time" events; we capitalize operating leases where their use is significant (e.g., in transportation and retail); and we convert inventory to FIFO accounting when LIFO costing is used. For more information on these adjustments and others, as well as additional background, please see "Morgan Stanley ModelWare (ver. 1.0): A Road Map for Investors," by Trevor Harris and team, August 2, 2004.

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## Analyst Certification

The following analysts hereby certify that their views about the companies and their securities discussed in this report are accurately expressed and that they have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report: Carrie Stevens.

## Important US Regulatory Disclosures on Subject Companies

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As of January 31, 2005, Morgan Stanley beneficially owned 1% or more of a class of common equity securities of the following companies covered in this report: Ameren Corporation, American Electric Power, CMS Energy, Calpine Corp., Cinergy, Consolidated Edison Inc, Constellation Energy, DTE Energy, Edison International, Energy East, Entergy Corp., Exelon Corp., FPL Group, FirstEnergy, PS Enterprise Group, Pinnacle West, SCANA Corporation, Southern Company and TECO Energy.

Within the last 12 months, Morgan Stanley managed or co-managed a public offering of securities of Puget Energy, CMS Energy, Consolidated Edison Inc, DPL Inc., DTE Energy, Edison International, Entergy Corp., FPL Group, FirstEnergy, Great Plains Energy and PPL Corp.

Within the last 12 months, Morgan Stanley has received compensation for investment banking services from American Electric Power, CMS Energy, Calpine Corp., Cinergy, Consolidated Edison Inc, Constellation Energy, DPL Inc., DTE Energy, Energy East, Entergy Corp., Exelon Corp., FPL Group, FirstEnergy, Great Plains Energy, Northeast Utilities, PG&E Corp., PPL Corp., PS Enterprise Group, Pepco Holdings, Inc., Sempra Energy, Southern Company, TECO Energy, TXU Corp. and Xcel Energy.

In the next 3 months, Morgan Stanley expects to receive or intends to seek compensation for investment banking services from Puget Energy, Alliant Energy Corp., Ameren Corporation, American Electric Power, CMS Energy, Calpine Corp., Cinergy, Consolidated Edison Inc, Constellation Energy, DPL Inc., DTE Energy, Edison International, Energy East, Entergy Corp., Exelon Corp., FPL Group, FirstEnergy, Great Plains Energy, Northeast Utilities, PG&E Corp., PPL Corp., PS Enterprise Group, Pinnacle West, Progress Energy Inc., SCANA Corporation, Sempra Energy, Southern Company, TECO Energy, TXU Corp. and Xcel Energy.

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Within the last 12 months, Morgan Stanley has either provided or is providing non-investment banking, securities-related services to and/or in the past has entered into an agreement to provide services or has a client relationship with the following companies covered in this report: Puget Energy, Alliant Energy Corp., Ameren Corporation, American Electric Power, CMS Energy, Calpine Corp., Cinergy, Consolidated Edison Inc, Constellation Energy, DPL Inc., DTE Energy, Energy East, Entergy Corp., Exelon Corp., FPL Group, FirstEnergy, Great Plains Energy, Northeast Utilities, PG&E Corp., PPL Corp., PS Enterprise Group, Pepco Holdings, Inc., Pinnacle West, Progress Energy Inc., SCANA Corporation, Sempra Energy, Southern Company, TECO Energy, TXU Corp. and Xcel Energy.

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Different securities firms use a variety of rating terms as well as different rating systems to describe their recommendations. For example, Morgan Stanley uses a relative rating system including terms such as Overweight, Equal-weight or Underweight (see definitions below). A rating system using terms such as buy, hold and sell is not equivalent to our rating system. Investors should carefully read the definitions of all ratings used in each research report. In addition, since the research report contains more complete information concerning the analyst's views, investors should carefully read the entire research report and not infer its contents from the rating alone. In any case, ratings (or research) should not be used or relied upon as investment advice. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations.

## Global Stock Ratings Distribution

(as of January 31, 2005)

Stock Rating Category	Coverage Universe		Investment Banking Clients (IBC)		
	Count	% of Total	Count	% of Total IBC	% of Rating Category
<b>Overweight/Buy</b>	647	35%	260	39%	40%
<b>Equal-weight/Hold</b>	845	45%	297	45%	35%
<b>Underweight/Sell</b>	378	20%	106	16%	28%
<b>Total</b>	1,870		663		

Data include common stock and ADRs currently assigned ratings. For disclosure purposes (in accordance with NASD and NYSE requirements), we note that Overweight, our most positive stock rating, most closely corresponds to a buy recommendation; Equal-weight and Underweight most closely correspond to neutral and sell recommendations, respectively. However, Overweight, Equal-weight, and Underweight are not the equivalent of buy, neutral, and sell but represent recommended relative weightings (see definitions below). An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley or an affiliate received investment banking compensation in the last 12 months.

## Analyst Stock Ratings

**Overweight (O).** The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

**Equal-weight (E).** The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

**Underweight (U).** The stock's total return is expected to be below the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

**More volatile (V).** We estimate that this stock has more than a 25% chance of a price move (up or down) of more than 25% in a month, based on a quantitative assessment of historical data, or in the analyst's view, it is likely to become materially more volatile over the next 1-12 months compared with the past three years. Stocks with less than one year of trading history are automatically rated as more volatile (unless otherwise noted). We note that securities that we do not currently consider "more volatile" can still perform in that manner.

Unless otherwise specified, the time frame for price targets included in this report is 12 to 18 months. Ratings prior to March 18, 2002: SB=Strong Buy; OP=Outperform; N=Neutral; UP=Underperform. For definitions, please go to [www.morganstanley.com/companycharts](http://www.morganstanley.com/companycharts).

## Analyst Industry Views

**Attractive (A).** The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark named on the cover of this report.

**In-Line (I).** The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark named on the cover of this report.

**Cautious (C).** The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark named on the cover of this report.

Stock price charts and rating histories for companies discussed in this report are also available at [www.morganstanley.com/companycharts](http://www.morganstanley.com/companycharts). You may also request this information by writing to Morgan Stanley at 1585 Broadway, 14th Floor (Attention: Research Disclosures), New York, NY, 10036 USA.

**Stock Price, Price Target and Rating History (See Rating Definitions)**

Puget Energy (PSD.N) - As of 2/10/05 in USD  
Industry : Electric Utilities



Stock Rating History: 8/11/00 : N; 3/18/02 : E/I; 12/6/02 : E/C  
Price Target History: No Price Target Assigned (NA)

Source: Morgan Stanley Research      Date Format : MM/DD/YY      Price Target - -      No Price Target Assigned (NA)  
Stock Price (Not Covered by Current Analyst) - -      Stock Price (Covered by Current Analyst) - -  
Stock Ratings abbreviated as below (Effective 3/18/02, ratings appear as Stock Ratings/Industry View) ♦  
Stock Ratings as of 3/18/02: Overweight (O) Equal-weight (E) Underweight (U) More Volatile (V) No Rating Available (NAV)  
Stock Ratings prior to 3/18/02: Strong Buy (SB) Outperform (OP) Neutral (N) Underperform (UP) No Rating Available (NAV)  
Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

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## Other Important Disclosures

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For a discussion, if applicable, of the valuation methods used to determine the price targets included in this summary and the risks related to achieving these targets, please refer to the latest relevant published research on these stocks. Research is available through your sales representative or on Client Link at [www.morganstanley.com](http://www.morganstanley.com) and other electronic systems.

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**INDUSTRY COVERAGE: ELECTRIC UTILITIES**

Company	Ticker	Rating as of	Price at 02/10/05	Company	Ticker	Rating as of	Price at 02/10/05		
Alliant Energy Corp.	LNT.N	U	10/28/02	\$26.94	Northeast Utilities	NU.N	E	11/25/03	\$18.97
Ameren Corporation	AEE.N	E	10/10/02	\$50.98	Pepco Holdings, Inc.	POM.N	E	03/18/02	\$22.65
American Electric Power	AEP.N	U	01/21/05	\$34.63	PG&E Corp.	PCG.N	O-V	06/16/03	\$35.84
Calpine Corp.	CPN.N	E-V	03/18/02	\$3.47	Pinnacle West	PNW.N	E	03/18/02	\$41.69
Cinergy	CIN.N	E	10/28/02	\$40.61	PPL Corp.	PPL.N	E	12/03/04	\$54.33
CMS Energy	CMS.N	U	01/17/03	\$11.30	Progress Energy Inc.	PGN.N	E	07/01/03	\$43.90
Consolidated Edison Inc	ED.N	E	11/05/02	\$44.60	PS Enterprise Group	PEG.N	NR	12/20/04	\$54.25
Constellation Energy	CEG.N	E	03/18/02	\$52.04	Puget Energy	PSD.N	E	03/18/02	\$24.00
DPL Inc.	DPL.N	E	03/18/02	\$25.55	SCANA Corporation	SCG.N	E	10/10/02	\$39.71
DTE Energy	DTE.N	O	09/24/04	\$44.75	Sempra Energy	SRE.N	E	09/13/04	\$39.91
Edison International	EIX.N	O	01/04/05	\$32.56	Southern Company	SO.N	E	03/18/02	\$33.52
Energy East	EAS.N	E	10/07/02	\$26.35	TECO Energy	TE.N	E-V	07/08/04	\$15.95
Entergy Corp.	ETR.N	O	03/18/02	\$70.35	TXU Corp.	TXU.N	NR	04/26/04	\$75.22
Exelon Corp.	EXC.N	NR	12/20/04	\$45.70	Xcel Energy	XEL.N	E	12/15/03	\$17.95
FirstEnergy	FE.N	E	12/01/04	\$40.92					
FPL Group	FPL.N	E	09/10/02	\$79.10					
Great Plains Energy	GXP.N	U	10/20/04	\$31.11					

*Stock ratings are subject to change. Please see latest research for each company.*

FEBRUARY 10, 2005

CUSIP #745310102

## PUGET ENERGY, INC.

(NYSE - PSD)

### Selling Off of the Value Recommended Lists – Appreciation/Income

**Price:** \$24.27

#### Earnings Per Share

FY03A	\$1.22
FY04A	\$1.26
FY05E	\$1.66

#### P/E Ratios

FY03A	19.9x
FY04A	19.3x
FY05E	14.6x

<b>Book Value</b>	\$15.96
<b>Share Count (mils)</b>	99.8
<b>Market Cap (bils)</b>	\$2.42
<b>TTM Revenue (mils)</b>	\$2.57
<b>Dividend:</b>	\$1.00
<b>Yield:</b>	4.1%
<b>52-Week Range:</b>	\$25-\$21
<b>FY End:</b>	Dec

<b>Time:</b>	9:40 a.m. (PST)
<b>DJIA</b>	10712.38

We are removing Puget Energy, Inc. from both the Value Recommended List – Appreciation and the Value Recommended List – Income and recommending that investors sell their shares. Although the stock's dividend remains stable this year and the stock price is slightly below the \$25 price target we previously set, we see several negative items likely to affect the company and its stock performance going forward.

We concede that the utility's financial results would improve with a return to "normal" weather conditions but we continue to see little evidence of improvement in the regulatory arena for the company despite management's comments to that effect. With our view that longer-term interest rates may rise over the next year and the company's limited financial flexibility given its relatively poor recent internal returns on investment, we feel it is best to sell the position and wait for further developments.

The company has a \$145 million rate increase proposal pending with Washington state regulators, which the regulatory staff has argued against, and which is expected to receive a final ruling in March. The pending decision could potentially move the stock down heavily, in our opinion, if the decision is negative as there was little apparent price reaction when the regulatory staff first opposed it in a public filing. In our opinion, upside to the stock on a decision would be limited unless the commissioners granted almost all the proposed increase. As weather continues to be warmer than average through January, the combination of poor regulatory news and potentially poor earnings during the critical winter period would likely cause the stock to pull back, in our opinion.

Additionally, the company is divesting its InfrastruX business, which led to a \$0.77 charge to 4Q04 earnings as management wrote down the value of its investment. Depending on the outcome of the sale and the general rate case, management has mentioned it may need to do a secondary equity offering later in the year. We do not feel the dividend is threatened in 2005, but if the company is required to do a secondary late in the year, the possibility of a dividend cut in 2006 does exist.

Puget currently trades at a slight premium to its peer average on 2005 earnings which is likely due to its higher-than peer group dividend.

We initially added PSD to the Value Recommended List – Appreciation on 9/28/93 and moved it to a HOLD on 2/16/95. We added PSD to the Value Recommended List – Income on 3/26/02 and moved it to a HOLD on 10/24/02.

*(Continued)*

**VALUATION**

We view Puget Energy stock as fully valued at its current level, which is close to our prior target price for the shares of \$25, or 15x our FY05 earnings estimate. Puget trades at a slight premium to a group of peer companies we assembled that are all combination gas and electric utilities.

	Ticker	Price	Div. Yield (%)	P/Book	P/Sales	P/EBITDA	P/E	P/E (est)
Pinnacle West Capital Corp.	PNW	\$41.79	4.55	NA	1.32	3.98	16.25	13.89
Xcel Energy Inc.	XEL	\$18.04	4.60	NA	0.86	3.89	14.18	14.23
Sempra Energy	SRE	\$39.51	2.53	2.10	1.05	4.74	11.00	11.27
Avista Corp.	AVA	\$17.63	2.95	1.13	0.74	3.74	24.25	13.73
PNM Resources Inc.	PNM	\$25.64	2.89	1.39	1.01	5.14	18.84	17.81
MDU Resources Group Inc.	MDU	\$27.05	2.66	NA	1.16	5.55	15.45	14.15
<b>AVERAGE</b>			<b>3.36</b>	<b>1.54</b>	<b>1.02</b>	<b>4.51</b>	<b>16.66</b>	<b>14.18</b>
Dow Jones Utility Average			2.97	2.29	1.23	NA	18.23	15.77
<b>Puget Energy Inc.</b>	<b>PSD</b>	<b>\$24.04</b>	<b>4.16</b>	<b>1.44</b>	<b>0.94</b>	<b>3.89</b>	<b>20.94</b>	<b>15.91</b>

Source: Factset, Bloomberg (2/9/05)

**RISKS**

Primary risks surrounding the stock include adverse regulatory rate case developments and rising third-party energy prices. While the PCA mechanism should allow the company to pass most of these costs to the customer, the mechanism must be renewed in 2006, creating more regulatory risk that it will be changed at some point in the future.

Puget Energy, Inc. is one of Washington state's largest utility companies. Through its subsidiary, Puget Sound Energy, it provides electricity to more than 940,000 customers and provides natural gas to more than 600,000 in western Washington. The company owns some fossil-fueled and hydroelectric plants and its InfrastruX Group specializes in energy management and infrastructure construction services. Headquarters: Bellevue, WA

Other public companies mentioned:

- Pinnacle West Capital Corp. (NYSE-PNW-\$41.81, not rated)
- Xcel Energy, Inc. (NYSE-XEL-\$18.00, not rated)
- Sempra Energy (NYSE-SRE-\$40.01, not rated)
- Avista Corp. (NYSE-AVA-\$17.63, HOLD)
- PNM Resources, Inc. (NYSE-PNM-\$25.91, not rated)
- MDU Resources Group, Inc. (NYSE-MDU-\$27.11, not rated)

## REQUIRED DISCLOSURES

The analyst or a member of the analyst's household has beneficial ownership in the securities of Puget Energy, Inc. in the form of a long position in such securities.

### ANALYST CERTIFICATION

By issuing this research report, each Ragen MacKenzie analyst whose name appears on the front page of this research report hereby certifies that: (i) the recommendations and opinions expressed in the research report accurately reflect the research analyst's personal views about any and all of the subject securities or issuers discussed herein and (ii) no part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in the research report.

### PRICE TARGET VALUATION METHODOLOGY AND RISKS

The methods used to determine the price target are generally based on a multiple of earnings, cash flow, revenue and/or historical and relative valuation multiples. Risks that could impede achievement of our price target include, but are not limited to, changes in economic and industry conditions, consumer and business spending patterns, as well as geo-political risks. When a price target is used, please refer to the Valuation and Risks section in the body of the report for additional discussion on the specific valuation methodology and related risk factors as they pertain to this analyst's investment thesis.

### RATING SYSTEM

**BUY** – Immediate purchase is recommended; the stock is expected to outperform the general market over the next 12-18 months.

**HOLD** – Holding the stock is recommended. The stock has moved out of our preferred buying range, but there is further upside to the share price; or stated objectives at the time of purchase have changed and share appreciation may take another 6-12 months.

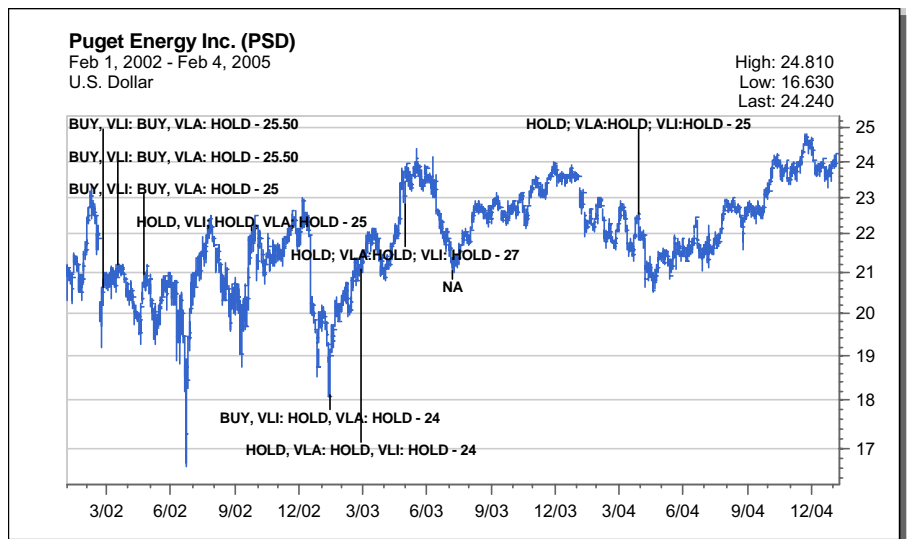
**SELL** – The stock has reached the stated price objective and appreciation has been achieved; or certain company fundamentals have changed which warrant investors selling the stock to avoid price decline.

### RATINGS ALLOCATIONS

Rating	% of covered companies with this rating	% for which IB Services have been provided
<i>Analyst Coverage</i>		
BUY	20%	0%
HOLD	73%	8%
SELL	8%	0%
<i>Value Recommended List—Appreciation</i>		
BUY	22%	0%
HOLD	61%	9%
SELL	17%	0%
<i>Value Recommended List—Income</i>		
BUY	43%	33%
HOLD	43%	33%
SELL	14%	0%
<i>Growth Recommended List</i>		
BUY	14%	0%
HOLD	71%	0%
SELL	14%	0%

Updated on 01/03/2005

### PRICE HISTORY



The price targets indicated in the chart above may be adjusted for stock splits. Where the price target was originally given as a range, the midpoint of the range has been used. Until July 8, 2002, Ragen MacKenzie used the following system for analyst ratings: Strong Buy (SB), Buy, Market Perform (MP), Underperform, Sell. The current rating system, explained above, has been in effect since July 9, 2002.

## OTHER DISCLOSURES

**INVESTMENT PRODUCTS:**      ▶ **NOT FDIC INSURED**      ▶ **NO BANK GUARANTEE**      ▶ **MAY LOSE VALUE**

**Additional Information on Subject Companies Mentioned Herein Is Available Upon Request.** Ragen MacKenzie is a division of Wells Fargo Investments, member NYSE/SIPC, a non-bank affiliate of Wells Fargo & Co. This is not a complete analysis of every material fact regarding any company, industry, or security. The information has been obtained from sources we consider to be reliable, but we cannot guarantee the accuracy. Opinions represent Ragen MacKenzie's judgment as of the date of the report and are subject to change without notice. Wells Fargo affiliates may issue reports or have opinions that are inconsistent with and reach different conclusions from this report.

Ragen MacKenzie - A Division of Wells Fargo Investments, LLC - 999 Third Avenue, Suite 4000 - Seattle, WA 98104

FEBRUARY 10, 2005

UTILITIES

## Puget Energy, Inc.

NYSE - PSD

*Risks Appear to Be Increasing Rather than Decreasing – Moving to Sell*

 ANALYST OPINION: **SELL**

 VALUE RECOMMENDED LIST—APPRECIATION/INCOME: **SELL/SELL**

### PRIMARY STOCK STATISTICS

FY End	Dec
52-Week Range	\$25-\$21
Market Cap (billion)	\$2.42
TTM Revenue (billion)	\$2.57
Shares Outstanding (million)	99.8
Book Value	\$15.96
Dividend/Yield	\$1.00/4.1%
Est. Sec. EPS Grth Rate	5%

 PRICE: **\$24.26**

 PRICE TARGET: **NA**

### EARNINGS ESTIMATES

Current Quarter

FY03A

FY04A

FY05E

PRIOR

-

-

-

\$1.66

CURRENT

-

\$1.22

\$1.26

\$1.66

P/E

-

19.9x

19.3x

14.6x

### KEY POINTS

- We are downgrading PSD to SELL (from Hold) as the risks surrounding the Company and the stock appear to be increasing rather than decreasing. Of the three major risks (weather, interest rates, and regulatory) affecting the stock price, none have shown much tangible progress over the past several months to support much upside in our opinion.
- With a decision upcoming this quarter on the Company's Washington state \$145 million rate filing, we are not confident that the Company will achieve meaningful rate relief given the regulatory staff's position (which argues for only ~\$28 million in its most recent update). We believe the stock could react negatively should the decision be significantly less than what the Company is requesting and therefore advise investors to reduce positions. We continue to favorably view management's focus on improving its relationship with its regulators as being favorable to shareholders.
- PSD reported 4Q04 EPS from continuing operations of \$0.59, ahead of consensus and up from EPS of \$0.44 in 4Q03 but quality of the earnings was poor in our opinion as \$0.11 of the change was due to lower taxes and increased Other Income rather than core utility income. Company pursuing divestiture of InfrastrucX and took a \$0.77 charge in 4Q04 to write-down the asset.
- Due to the upcoming decision on the rate case, no EPS guidance was given for FY05. We maintain our \$1.66 FY05 EPS estimate.

### SUMMARY AND STOCK OPINION

With Puget Energy's stock price trading less than a dollar below our prior target price of \$25, we view the stock as close enough to fully valued that we are moving the stock to an analyst SELL (concurrent with our changing the rating to a SELL on the Ragen MacKenzie Value Recommended List – Appreciation and Value Recommended List – Income). With near-term risk increasing due to the upcoming power cost rate decision in early March and longer-term dynamics (such as interest rates) which may negatively affect the stock price, we are no longer comfortable with advising investors to hold the stock.

(Continued)

Of the three main variables we see directly affecting the stock (the weather, the interest rate environment, and the regulatory environment), none appear favorably positioned at the moment. Much like December, January was warmer than normal which will likely continue to weigh on 1Q05 earnings. (While the PCA mechanism limits the earnings hit to the Company from weather, it doesn't fully eliminate it.)

Our view on interest rates is that longer-term rates are likely to rise this year in response to the Federal Reserve's tightening at the short-end of the rate curve. This in turn will raise the utilities borrowing costs and reduce the attractiveness of the stock's current dividend (which we continue to see as stable through 2005).

With regards to regulators, we continue to look for more tangible evidence supporting management's assurances of a better regulatory relationship as the current disparity between the company and the regulatory Staff in the general rate case gives little evidence of it, in our opinion. According to the latest filings and after a partial settlement (that did very little to close the monetary gap between the parties), the Company and the regulatory Staff appear to still have disagreements over about \$100 million in costs (approximately 78% of the requested amount).

#### 4Q04 EARNINGS RESULTS

PSD reported 4Q04 EPS from continuing operations of \$0.59, which was three cents ahead of consensus estimates and up from \$0.44 in 4Q03. Earnings quality however was low in our opinion as \$0.11 of the difference was due to lower taxes and increased "other income". The core utility itself performed pretty much within expectations and management's previous guidance.

As a result of the past two years' underperformance of the InfrastrucX business, management has decided to divest the business and it was classified as discontinued in 4Q04 results. As part of the annual evaluation of goodwill impairment, the Company took a \$0.77 non-cash charge to write down approximately 60% of the carrying value of the investment in InfrastrucX in 4Q04, causing 4Q04 GAAP earnings to come in at a loss of \$0.16.

During the conference call, management indicated that capex spending was going to need to increase going forward and that delays caused by the regulatory process (increased maintenance and operations expenditures as well as increases in depreciation expense not included in the recent rate case) was likely to subtract \$0.15 in EPS in 2005 (though likely to be offset eventually via a later rate case filing). However, due to the uncertainty regarding the pending general rate case, management deferred giving any EPS guidance for the year. We are making no adjustment to our FY05 EPS estimate of \$1.66 at this point.

The subject of doing a secondary equity offering was brought up during the conference call but management indicated that the need, timing and amount of any secondary would be highly dependent on 1) outcome of the general rate case in WA and 2) how much the Company can get for InfrastrucX (management expects to be able to fully divest it in 2005). Our current EPS estimates do not include the effect of any potential secondary equity offering due to the high degree of uncertainty surrounding it.

#### VALUATION

We view Puget Energy shares as fully valued at its current level which is close to our previous target price of \$25, or 15x our FY05 earnings estimate.

#### RISKS

Primary risks surrounding the stock include adverse regulatory rate case developments and rising third-party energy prices. While the PCA mechanism should allow the Company to pass on most of these costs to the customer, the mechanism must be renewed in 2006, creating more regulatory risk that it will be changed at some point in the future.

*(Continued)*

Puget Energy, Inc. is one of Washington state's largest utility companies. Through its subsidiary, Puget Sound Energy, it provides electricity to more than 940,000 customers and provides natural gas to more than 600,000 in western Washington. The company owns some fossil-fueled and hydroelectric plants and its InfrastruX Group specializes in energy management and infrastructure construction services. Headquarters: Bellevue, WA

*Other public companies mentioned:*

Pinnacle West Capital Corp. (NYSE-PNW-\$41.81, not rated)

Xcel Energy, Inc. (NYSE-XEL-\$18.00, not rated)

Sempra Energy (NYSE-SRE-\$40.01, not rated)

Avista Corp. (NYSE-AVA-\$17.63, HOLD)

PNM Resources, Inc. (NYSE-PNM-\$25.91, not rated)

MDU Resources Group, Inc. (NYSE-MDU-\$27.11, not rated)

**S&P 500: 1194.12**

**REQUIRED DISCLOSURES**

The analyst or a member of the analyst’s household has beneficial ownership in the securities of Puget Energy, Inc. in the form of a long position in such securities.

**ANALYST CERTIFICATION**

By issuing this research report, each Ragen MacKenzie analyst whose name appears on the front page of this research report hereby certifies that: (i) the recommendations and opinions expressed in the research report accurately reflect the research analyst’s personal views about any and all of the subject securities or issuers discussed herein and (ii) no part of the research analyst’s compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in the research report.

**PRICE TARGET VALUATION METHODOLOGY AND RISKS**

The methods used to determine the price target are generally based on a multiple of earnings, cash flow, revenue and/or historical and relative valuation multiples. Risks that could impede achievement of our price target include, but are not limited to, changes in economic and industry conditions, consumer and business spending patterns, as well as geo-political risks. When a price target is used, please refer to the Valuation and Risks section in the body of the report for additional discussion on the specific valuation methodology and related risk factors as they pertain to this analyst’s investment thesis.

**RATING SYSTEM**

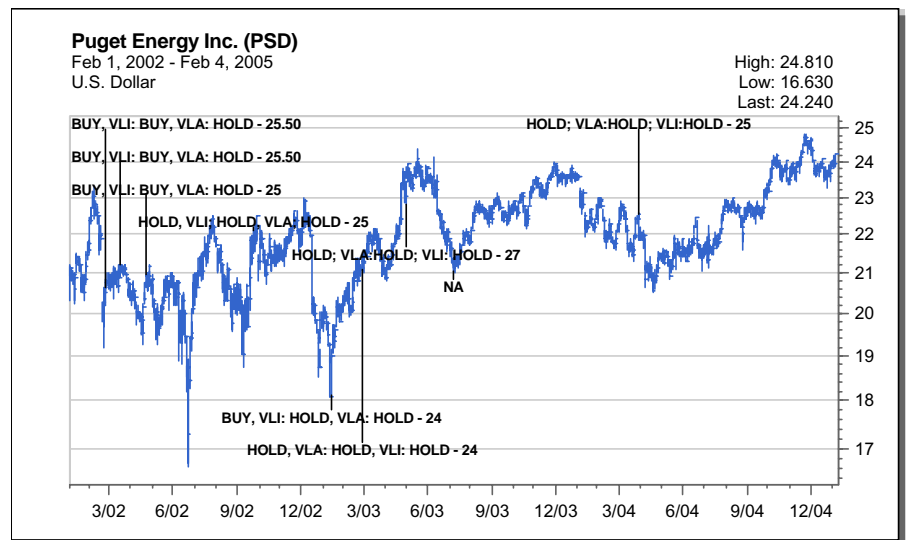
**BUY** – Immediate purchase is recommended; the stock is expected to outperform the general market over the next 12-18 months.  
**HOLD** – Holding the stock is recommended. The stock has moved out of our preferred buying range, but there is further upside to the share price; or stated objectives at the time of purchase have changed and share appreciation may take another 6-12 months.  
**SELL** – The stock has reached the stated price objective and appreciation has been achieved; or certain company fundamentals have changed which warrant investors selling the stock to avoid price decline.

**RATINGS ALLOCATIONS**

Rating	% of covered companies with this rating	% for which IB Services have been provided
<i>Analyst Coverage</i>		
BUY	20%	0%
HOLD	73%	8%
SELL	8%	0%
<i>Value Recommended List—Appreciation</i>		
BUY	22%	0%
HOLD	61%	9%
SELL	17%	0%
<i>Value Recommended List—Income</i>		
BUY	43%	33%
HOLD	43%	33%
SELL	14%	0%
<i>Growth Recommended List</i>		
BUY	14%	0%
HOLD	71%	0%
SELL	14%	0%

Updated on 01/03/2005

**PRICE HISTORY**



The price targets indicated in the chart above may be adjusted for stock splits. Where the price target was originally given as a range, the midpoint of the range has been used. Until July 8, 2002, Ragen MacKenzie used the following system for analyst ratings: Strong Buy (SB), Buy, Market Perform (MP), Underperform, Sell. The current rating system, explained above, has been in effect since July 9, 2002.

**OTHER DISCLOSURES**

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# UBS Investment Research

## Puget Energy Inc.

### A Mixed Bag

#### ■ Quarter Little Ahead of Estimates

Puget realized a 39% increase in recurring fourth quarter EPS, to \$0.61 from \$0.44 in 4Q03. The results were \$0.02 above our est. of \$0.59 and \$0.05 above consensus of \$0.56. For the year, Puget realized a 34% increase in recurring EPS, to \$1.55 from \$1.16 in 2003.

#### ■ Lowering 2005 and 2006 EPS Estimates

We are lowering our 2005E EPS to \$1.55, from \$1.70, to reflect the earnings lag due to \$400 million of capex at the utility in 2005. The co. has not yet decided on the timing or mechanism of recovery. We also are reducing our 2006 est. to \$1.70, from \$1.85, to reflect the aforementioned earnings lag and likely share dilution to finance the wind acquisitions.

#### ■ Magnitude of Infrastrux Impairment was Disappointing

While welcoming mgmt's strategic decision to sell Infrastrux the size of impairment reduces our expectation of sales proceeds and increases the scale of equity issuance required to finance wind acquisitions.

#### ■ Valuation: See Little Upside

Our 12-mth PT of \$24 (derived using DCF) implies a 14.1x PE on new 2006E EPS, roughly in-line with peers. While new wind generation assets support above average EPS growth at Puget, our view on the stock is tempered by several key risks that the co. faces including regulatory risks, Least Cost Plan execution risks, and high leverage.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,613	2,798	-
EBIT	377	418	436	456	-
Net income (UBS)	110	155	157	172	-
EPS (UBS, US\$)	1.16	1.55	1.55	1.70	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	16.7	16.3	-
ROIC (EBIT) %	-	9.3	9.5	9.9	-
EV/EBITDA x	-	6.9	6.7	6.5	-
PE (UBS) x	-	14.6	15.5	14.1	-
Dividend yield %	-	4.4	4.2	4.2	-

Source: UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$24.00 on 10 Feb 2005

Ronald J. Barone	Shalini Mahajan, CFA	Shneur Gershuni, CFA
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Electric Utilities

Rating	<b>Neutral 2</b> <i>Unchanged</i>
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Price target	US\$24.00 <i>Unchanged</i>
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Price	US\$24.00
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RIC: PSD.N BBG: PSD US

11 February 2005

#### Trading data

52-wk. range	US\$24.73-20.54
Market cap.	US\$2.39bn
Shares o/s	99.7m
Free float	80%
Avg. daily volume ('000)	206
Avg. daily value (US\$m)	4.9

#### Balance sheet data 12/05E

Shareholders' equity	US\$1.77bn
P/BV (UBS)	1.3x
Net cash (debt)	(US\$2.60bn)

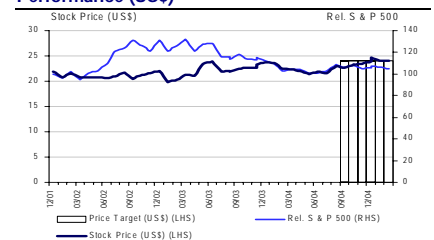
#### Forecast returns

Forecast price appreciation	+0.0%
Forecast dividend yield	4.2%
Forecast stock return	+4.2%
Market return assumption	8.3%
Forecast excess return	-4.1%

#### EPS (UBS, US\$)

	12/05E		12/04	12/04
	From	To	Cons.	Actual
Q1E	-	0.71	0.67	0.67
Q2E	-	0.17	0.17	0.16
Q3E	-	0.09	0.11	0.11
Q4E	-	0.60	0.60	0.61
12/05E	1.70	1.55	1.68	
12/06E	1.85	1.70	1.81	

#### Performance (US\$)



Source: UBS

[www.ubs.com/investmentresearch](http://www.ubs.com/investmentresearch)

#### ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 7

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## Earnings Summary

**4Q04 Review:** Puget realized a 39% increase in recurring fourth quarter diluted EPS, to \$0.61 from \$0.44 in 4Q03. The results were \$0.02 above our estimate of \$0.59 and \$0.05 above the Street consensus estimate of \$0.56. Year-over-year, results were positively impacted by an increase in electric margin due to absence of excess power costs associated with the power cost adjustment (PCA) mechanism, lower income tax expense and higher other income. These positives were partially offset by lower gas volumes due to warmer than normal weather and higher depreciation expense.

**2004 Review:** For the year, Puget realized a 34% increase in recurring diluted EPS, to \$1.55 from \$1.16 in 2003. The results were \$0.05 above our estimate of \$1.50 and \$0.03 above the Street consensus estimate of \$1.52. Year-over-year, results were positively impacted by an increase in electric margin due to absence of excess power costs associated with the PCA mechanism and lower interest expense, partially offset by additional shares outstanding and higher depreciation expense.

Please note, our recurring 2004 EPS excludes a \$0.23 per share disallowance related to the Tenaska project and a \$0.77 per share charge related to the Infrastrux valuation impairment and, hence, differs from the \$0.55 GAAP EPS reported by the company. We would also like to note that our 2003 EPS excludes a \$0.06 per share one-time tax benefit and, hence, differs from the \$1.22 GAAP EPS reported by the company.

**2005 EPS Guidance:** Management intends to issue 2005 EPS guidance after the Washington Utilities and Transportation Commission (WUTC) rules on Puget Sound Energy's (PSE) pending electric and gas case. PSE requested a \$99.8 million and a \$46.2 million rate increase for electric and gas customers, respectively. A ruling is expected no later than March 5, 2005.

**Infrastrux Asset Impairment:** The company completed its strategic review of Infrastrux and has determined that the business no longer fits its core strategy and, hence, intends to monetize the asset. As a result of ongoing challenges in Infrastrux's core business operations, the company took a \$76.6 million non-cash impairment charge in 4Q04, lowering the book value to \$33.4 million from \$110 million.

**Wind Update:** Management provided an update with respect to the two recently announced wind power projects – the 150 MW Hopkins Ridge project and the 160 MW Wild Horse project. The Hopkins Ridge project has been expeditiously reviewed and permits are pending. The Bonneville Power Administration (BPA) has facilitated transmission service to this project allowing for a December 2005 on-line target date. The Wild Horse project will likely be completed by the end of 2006; progress in the permitting process has

also been made and the plant is expected to use the existing PSE transmission once it comes on-line.

## Our View

Our reaction to Puget's quarterly results is a bit mixed. Earnings came in slightly better than expected, no doubt aided by the strong electric retail sales trend the utility is experiencing on the back of regional economic strength. The decision to sell Infrastrux was also welcome news given the onerous cash requirements at the utility. However, we were disappointed by the size of the impairment charge that Infrastrux had to take, which greatly reduces our expectation of what that business could be sold for. Thus we believe an equity issuance to finance the wind acquisition is more probable and imminent than our earlier expectation. Another disappointment was the revelation in the conference call that the utility faces an earnings lag in recovering its capital investments in 2005. The company has not yet decided on the timing or the mechanism of the cost recovery, but this only adds to a plethora of regulatory issues that are either pending or forthcoming at the utility.

While the addition of new generation assets to rate-base supports our thesis of above average earnings growth at Puget over the intermediate term, our view on the stock is somewhat tempered by several key risks that face the company, including the possibility of an unfavorable rate case decision, Least Cost Plan execution risks, and still high leverage (leverage fell to 60% at the end of 2004).

## Lowering 2005 and 2006 EPS Estimates

We are lowering our recurring 2005 EPS estimate to \$1.55, from \$1.70, to reflect the earnings lag resulting from the impact of \$400 million of capex at the utility in 2005 (which in itself is higher than our initial \$345 million capex estimate). PSE will need to file with the WUTC to recover the costs associated with this capital investment. The company has not decided on the timing or mechanism of recovery, hence, introducing an earnings lag of \$0.15 per share. Out of this, \$0.10 is attributable to higher depreciation and \$0.05 to higher O&M. Please note, the outcome of the pending general rate case, sale of Infrastrux, and mode of financing of wind projects (possible share dilution if equity issuance completed in 2005) could materially affect our 2005 estimates. The Street consensus for 2005 is \$1.68 (reflecting a range of \$1.50 – 1.83).

We are also lowering our 2006 EPS estimate to \$1.70, from \$1.85, to account for the aforementioned earnings lag resulting from the 2005 capex and share dilution resulting from our expectation that Puget will need to issue equity to finance the wind projects. Again, our estimates could be impacted by the timing of cost recovery and the actual size of a potential equity offering. The Street consensus estimate for 2006 currently stands at \$1.81, reflecting a range of \$1.70 – 1.89.

## Valuation

Our 12-month price target of \$24 per share is derived using a DCF analysis. This implies a 14.1x PE on our recurring 2006 EPS or in-line with peers. Price movement to \$24 per share – when combined with the current \$1.00/share annual dividend (or 4.2% yield) – suggests a 4.2% total return potential.

## Key 4Q04 Drivers

**Puget Sound Energy (PSE)**, the utility, realized a 34% increase in fourth quarter recurring EPS, to \$0.59 from \$0.44 in 4Q03. The increase was led by higher electric margins, which includes the electric rate tariff increase, effective May 2004, to reflect the Frederickson acquisition (\$0.08). Other positives include lower income tax expense (\$0.05) and lower interest expense (\$0.02). The non-regulated business at the utility benefited from gains on property sales (\$0.06). These positives were partially offset by a decrease in gas margin primarily due to warmer than normal weather (\$0.02), higher depreciation expense (\$0.02), the impact of share dilution (\$0.01), and other (\$0.01).

Electric retail sales were roughly flat quarter-over-quarter despite a 2.4% increase in customers. This was led by 0.6% and 0.5% increase in commercial and industrial sales, respectively, offset by a 0.2% decline in residential sales. Gas volumes declined 4.3%, led by a 6% decline in residential volumes. Commercial and transportation volumes also fell 3.1% and 2.6%, respectively. The only bright spot was a 5.4% increase in industrial volumes but this was not enough to offset the large decline in residential volumes. The quarter-over-quarter decline in gas volumes can be partially explained by 3% warmer weather versus the year-ago quarter. On the positive side, new accounts grew 4.1% compared with 4Q03.

**Infrastrux** realized a 100% increase in recurring 4Q diluted EPS, to \$0.02 from \$0.01 in 3Q03. Infrastrux benefited from a 20% revenue increase over the year-ago quarter.

## Key 2004 Drivers

**Puget Sound Energy (PSE)**, the utility, realized a 28% increase in recurring diluted EPS, to \$1.49 from \$1.16 in 2003. The increase was led by an increase in electric margin in 2004 (\$0.23) due to PSE hitting the cap for the PCA mechanism in 2004. Electric margins were also positively impacted by \$0.04 due to a rate increase in May 2004 for Frederickson plant addition. Other positive impacts included lower interest expense and absence of the preferred stock dividend (\$0.14), the absence of the venture capital impairment (\$0.04) and lower income tax expense (\$0.03). These positives were partially offset by additional shares outstanding (\$0.06), higher depreciation expense (\$0.06), other (\$0.02), and lower gas margin (\$0.01).

Electric retail sales increased 1.5% due to strong electric customer growth of 2.2%. Commercial and residential sales increased 2.8% and 1.9%, respectively. Industrial sales declined 1.5% year-over-year. PSE continued to experience strong gas customer growth of 3.7%, however, gas volumes declined 1.5% primarily due to warmer than normal weather in 2004. The decline in gas volumes was led by lower transportation and residential volumes of 3.7% and 2.2%, respectively, partially offset by an increase of 4.0% and 0.7% in industrial and commercial volumes, respectively. In 2004, weather was 8% warmer than normal and 2% warmer than 2003.

**Infrastrux** realized recurring 2004 diluted EPS of \$0.06, up from \$0.02 in 2003. These results exclude the impact of the \$77.6 million impairment recorded in 4Q04, to reflect the ongoing challenges in the utility construction services sector.

## ■ Puget Energy Inc.

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. InfrastruX provides infrastructure construction services to the electric and gas utility industries.

## ■ Statement of Risk

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. The utility has recently filed a general electric and gas rate case to request a \$128 million rate increase. However, the WUTC might not award the entire rate increase. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.

### ■ Analyst Certification

Each research analyst primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.

## Required Disclosures

This report has been prepared by UBS Securities LLC, an affiliate of UBS AG (UBS).

### UBS Investment Research: Global Equity Ratings Definitions and Allocations

UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	36%	32%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	53%	35%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	29%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 31 December 2004.

### KEY DEFINITIONS

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

**Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

**Rating/Return Divergence (RRD)** This qualifier is automatically appended to the rating when stock price movement has caused the prevailing rating to differ from that which would be assigned according to the rating system and will be removed when there is no longer a divergence, either through market movement or analyst intervention.

### EXCEPTIONS AND SPECIAL CASES

**US Closed-End Fund ratings and definitions are:** Buy: Higher stability of principal and higher stability of dividends; Neutral: Potential loss of principal, stability of dividend; Reduce: High potential for loss of principal and dividend risk.

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**Core Banding Exceptions (CBE):** Exceptions to the standard +/-10% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Companies Mentioned table in the relevant research piece.

### Companies mentioned

Company Name	Reuters	Rating	Price
<b>Puget Energy Inc.</b> <sup>4,5,6a,6b,6c,7,16</sup>	PSD.N	Neutral 2	US\$24.00

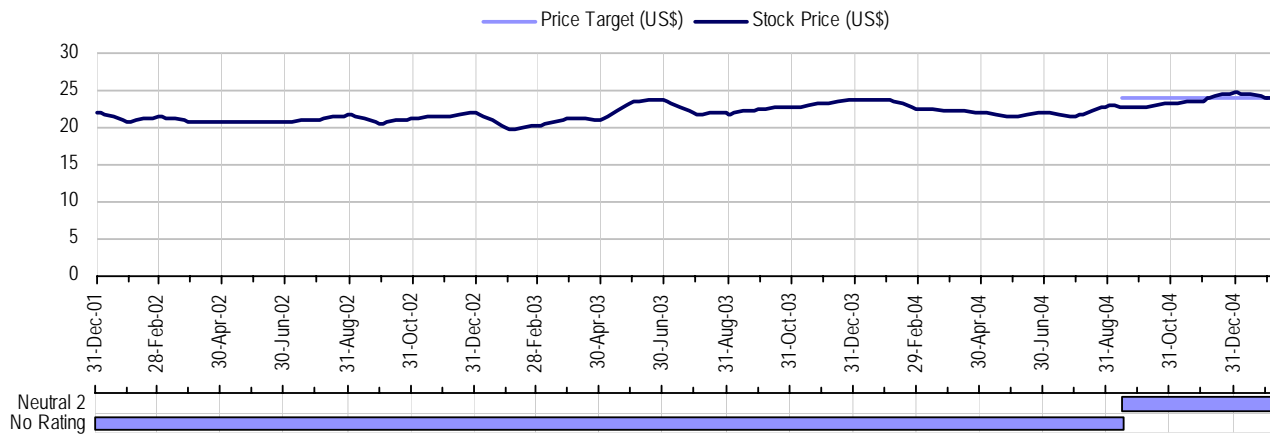
Price(s) as of 10 February 2005. Source: UBS.



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Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

**Puget Energy Inc. (US\$)**



Source: UBS; as of 10 February 2005.

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**PUGET ENERGY, INC.**

PSD – NYSE

February 11, 2005

**Rating:****NEUTRAL****Price:** (2/10/05) \$24.00**Price Targets:**

12-18 month: \$24

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

406.791.7230

jbellessa@dadco.com

FY (Dec)	2004A*	2005E	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,568.8	\$2,564.1	0%	\$2,507.4	-2%
Previous	\$2,584.8	\$2,768.8		\$2,902.2	
Price/Revenue ratio	.9x	.9x		1.0x	
<b>EPS Revised</b>	<b>\$0.55</b>	<b>\$1.53</b>	177%	<b>\$1.70</b>	11%
Previous	\$1.25	\$1.60		\$1.76	
Price/EPS ratio	43.6x	15.7x		14.1x	
<b>EBITDA (\$M)</b>	\$542.8	\$666.6	23%	\$703.3	5%
EV/EBITDA ratio	9.2x	7.5x		7.1x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05E	<b>\$0.69</b>	\$0.70	\$802.8	NC	\$216.4
6/30/05E	<b>\$0.17</b>	\$0.16	\$547.6	NC	\$133.7
9/30/05E	<b>\$0.06</b>	\$0.13	\$438.9	\$545.2	\$113.0
12/31/05E	<b>\$0.60</b>	\$0.61	\$774.7	\$873.1	\$203.5

\*See detail of footnote on page 2.

**Valuation Data**

Long-term growth rate (E)	5%
Total Debt/Cap (9/30/04)	61.2%
Cash per share (9/30/04)	\$0.25
Book value per share (9/30/04)	\$16.67
Dividend (yield)	\$1.00 (4.2%)
Return on Equity (T-T-M)	3%

**Trading Data**

Shares outstanding (M)	99.7
Market Capitalization (\$M)	\$2,392
52-week range	\$20.51 - \$24.81
Average daily volume (3 mos.) (K)	290
Float	100%
Index Membership	S&P 400 MidCap

**Impairment Charge Taken for InfrastruX, Which Is Being Divested. Lowering Estimates, but Maintaining NEUTRAL Rating.**

- Puget Energy reported a 4Q'04 loss of \$0.16 per share compared to a profit of \$0.44 per share in 4Q'03. We were forecasting \$0.54 per share. The negative variance from our forecast is primarily explained by an impairment charge of \$0.77 per share to writedown the goodwill of InfrastruX, the company's unregulated utility construction services subsidiary.
- Regulated utility 4Q'04 EPS of \$0.58 compared to \$0.45 a year earlier, and our forecast of \$0.52. Had it not been for tax changes which added \$0.05 per share, quarterly operating EPS would have been very close to our forecast.
- Excluding the InfrastruX impairment charge, non-regulated business 4Q'04 EPS was \$0.02 compared to a loss of \$0.01 a year ago, and our forecast of \$0.02.
- To reflect more regulatory lag than we previously assumed, we are lowering our 2005 EPS estimate of \$1.60 to \$1.53. This is based on an assumption of normal weather, a \$70 million annualized increase in electric and gas rates in Washington starting on or about March 1, and a mid-2005 divestiture of InfrastruX. Management has not yet provided 2005 EPS guidance. Our 2006 EPS forecast is lowered from \$1.76 to \$1.70.
- We are maintaining our 12-18 month target price of \$24, or 14.9x the average of our 2005 and 2006 EPS estimates. With the share price near this target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.2%.

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*Includes a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax

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**Operating Results Near Expectations**

Puget Energy reported a 4Q'04 loss of \$0.16 per share compared to a profit of \$0.44 per share in 4Q'03. We were forecasting \$0.54 per share. The negative variance from our forecast is primarily explained by an impairment charge of \$0.77 per share to writedown the goodwill of InfrastruX, the company's unregulated utility construction services subsidiary.

Puget Energy took this 4Q'04 charge of \$76.6 million after tax, or \$0.77 per share, to remove \$91.2 million of InfrastruX's \$134.7 million in goodwill. In other terms, Puget's \$110 million investment in InfrastruX was reduced by \$76.6 million. Since ownership in InfrastruX no longer fits its strategy, Puget said it will attempt to monetize its investment in this business through a sale or third party recapitalization. While it is uncertain how much this divestiture will fetch, Puget says the sales proceeds will be invested in the regulated utility.

**Tax Benefits Help Utility**

Regulated utility 4Q'04 EPS of \$0.58 compared to \$0.45 a year earlier, and our forecast of \$0.52. Utility results were aided by a lower tax rate (40.5% vs. 43.1%) and a \$0.01 per share non-recurring federal income tax benefit. Had it not been for these tax changes, which added \$0.05 per share, quarterly operating EPS would have been very close to our forecast.

Besides the tax benefits, the increase in regulated utility EPS reflected the following benefits: improved electric margin (+\$0.08/sh.) due to the tariff increase implemented to rate base the Frederickson 1 plant acquisition on May 24, 2004, and despite the disallowance mentioned below; and lower interest expense (+\$0.02/sh.) due to the redemption of high cost debt and preferred stock over the past year. These positive benefits were partially offset by the following subtractions: a decrease in gas margin (-\$0.02/sh.) due to slightly warmer temperatures and lower customer usage in response to higher natural gas prices; a Tenaska plant-related disallowance (-\$0.02/sh.); an increase in depreciation and amortization expense (-\$0.02/sh.); and the impact of share dilution (-\$0.01/sh.) from the issuance of approximately \$100 million of common stock in 4Q'03.

Excluding the InfrastruX impairment charge, non-regulated business 4Q'04 EPS was \$0.02 compared to a loss of \$0.01 a year ago, and our forecast of \$0.02. In the year ago period, a writedown of a non-utility venture capital investment reduced EPS by \$0.06.

Note that we separate earnings between regulated and non-regulated activities to more clearly keep tabs of the electric and gas business, having found over time that the timing of the utility's non-regulated activities is not predictable. This means we remove non-regulated earnings from the company's utility, Puget Sound Energy, and combine them with the non-regulated results of InfrastruX, calling them "non-regulated" earnings.

**Mild Temperatures Offset Customer Growth**

Quarterly electric revenues of \$405 million climbed \$18 million, or 5%. This increase was due primarily to a \$9 million improvement in retail sales and \$9 million increase in wholesale, transportation, and other revenues. Retail sales rose because of the May 24, 2004 rate increase. Retail volumes were flat, as 2.4% customer growth was offset by reduced usage because temperatures were 3% warmer than year ago.

After deducting from electric revenues the costs of generating and purchasing electric energy, Puget Sound Energy had electric margins of \$188 million during 4Q'04. These electric margins were up \$12 million, or 7%, primarily because the electric utility was not adversely impacted by excess power costs, as was the case a year earlier. Also helping the electric margin was an electric rate increase effective May 24, 2004 and customer growth. These electric margin beneficiaries were partially offset by a \$2.8 million pretax, or \$0.02 per share, regulatory disallowance in connection with gas supply costs for the Tenaska generating project.

Quarterly gas revenues of \$285 million rose \$33 million, or 13%, primarily due to higher tariffs under the current Purchased Gas Adjustment mechanism to recover higher purchased gas costs. Gas revenues also rose due to 4.1% customer growth, and an improved economy in the company's service territory in Washington, which was more than offset by slightly warmer temperatures and lower usage in response to higher natural gas prices. Heating-

degree days from October 1, 2004 through December 31, 2004 in the company's service territory were 5% warmer than normal and 3% warmer than a year earlier. After deducting from gas revenues the costs of gas sales to retail and transportation customers, gas margins were \$79 million in 4Q'04, which were down \$4 million, or 4%, from 4Q'03.

Revenues at InfrastruX of \$102 million rose \$17 million, or 20%. The company did not initially provide an explanation for this improvement. Excluding the impairment charge, InfrastruX reported 4Q'04 net income of \$1.9 million, or \$0.02 per share, up from \$0.7 million, or \$0.01 per share, a year earlier.

**Lowering Estimates, but  
Maintaining Rating In Front of  
Rate Case Decision**

Management provided no earnings guidance for 2005, electing to wait for a general rate case decision by the Washington Utilities and Transportation Commission (WUTC) before providing an EPS outlook. Results for 2005 will be significantly impacted by that decision which is scheduled to be handed down no later than March 5, 2005. The company has requested a \$149.5 million increase in rates. The staff of the WUTC has recommended a rate increase of \$29.5 million.

To reflect more regulatory lag than we previously assume, we are lowering our 2005 EPS estimate of \$1.60 to \$1.53. This is based on an assumption of normal weather and a \$70 million annualized increase in electric and gas rates in Washington starting on or about March 1, and a mid-2005 divestiture of InfrastruX. While temperatures in January started off cold, a mid-January thaw sent temperatures higher, and temperatures for the entire month averaged 7% warmer than normal and 8% warmer than a year ago. Our 2006 EPS forecast is lowered from \$1.76 to \$1.70.

We are maintaining our 12-18 month target price of \$24, or 14.9x the average of our 2005 and 2006 EPS estimates. Over the past decade, the stock of PSD has traded at a median 14.6x multiple of year-forward earnings. With the share price near this target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.2%.

James L. Bellessa Jr., CFA  
Vice President Research  
406.791.7230

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

**Assets****Utility Plant:**

	2000	2001	2002	2003	9/30/2004
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,361,504
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,845,141
Common plant	351,051	362,670	378,844	390,622	406,395
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,424,162)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,188,878

**Other Property and Investments:**

Investment in Bonneville Exchange Power Contract	58,189	54,663	51,136	47,609	44,964
Goodwill, net	45,655	102,151	125,555	133,302	133,069
Intangibles, net		16,059	18,652	18,707	17,239
Non-utility property and equipment, net		48,369	80,855	91,932	95,024
Other	188,453	96,007	101,932	110,543	108,703
Total other property and investments	292,297	317,249	378,130	402,093	398,999

**Current Assets:**

Cash	36,383	92,356	176,669	27,481	21,211
Restricted cash			18,871	2,537	3,777
Accounts receivable, net					
Less: Allowance for doubtful accounts					
Total accounts receivable	343,108	279,321	279,623	227,115	202,423
Unbilled revenues	211,784	147,008	112,115	131,798	75,928
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	117,081
Purchased gas receivable	96,050	37,228			18,172
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	33,386
Taxes receivable					
Prepayments and other	11,607	11,277	11,323	12,200	23,360
Total current assets	797,933	660,838	672,744	493,852	495,338

**Long-Term Assets:**

Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	135,662
PURPA buyout costs	243,071	244,635	243,584	227,753	215,369
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	25,076
Power cost adjustment mechanism				3,605	
Other	177,609	239,941	269,876	315,739	386,090
Total Long-term assets	628,030	680,909	690,388	698,513	762,197

<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,845,412</b>
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**Capitalization and Liabilities****Capitalization:**

Common stock	\$859,038	\$870	\$936	\$991	\$997
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,617,164
Earnings reinvested in the business	92,673	32,229	36,396	58,217	54,462
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(11,348)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,661,275
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,218,042
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,161,456

Minority interest in equity of a consolidated subsidiary

**Current Liabilities:**

Accounts payable	410,619	167,426	205,619	214,357	165,052
Short-term debt	378,316	348,577	47,295	13,893	24,511
Current maturities of long-term debt	19,000	119,523	73,206	246,829	90,305
Purchased gas liability	0	0	83,811	11,984	
Accrued expenses:					
Taxes	103,996	70,708	62,562	77,451	26,568
Salaries and wages	17,445	14,746	11,441	12,712	12,594
Interest	43,955	42,505	37,942	32,954	41,018
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	4,270
Tenaska disallowance reserve					11,212
Other	26,685	46,178	47,761	46,378	46,498
Total current liabilities	1,000,016	844,808	572,047	660,194	422,028
Deferred Income Taxes	608,185	605,315	730,675	755,235	808,991
Other Deferred Credits	132,869	196,339	267,458	340,893	440,816
Commitments and Contingencies	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	0
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,845,412</b>

## PUGET SOUND ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)	4Q03	2003	1Q04	2Q04	3Q04	4Q04	2004	1Q05E	2Q05E	3Q05E	4Q05E	2005E	2006E
<b>OPERATING REVENUES:</b>													
Electric	\$386,510	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$1,423,033	\$407,946	\$320,446	\$340,097	\$439,282	\$1,507,771	\$1,584,770
Gas	251,524	634,230	275,692	119,479	89,432	284,703	769,306	314,038	130,949	97,335	333,876	876,198	916,585
Other	89,815	347,830	75,283	93,369	102,850	104,971	376,473	80,850	96,250	1,500	1,500	180,100	6,000
Total operating revenues	727,849	2,382,803	743,470	515,939	514,951	794,452	2,568,812	802,834	547,646	438,932	774,658	2,564,069	2,507,355
<b>OPERATING EXPENSES:</b>													
Energy costs:													
Purchased electricity	201,927	714,469	196,367	173,847	147,589	205,764	723,567	208,052	147,405	163,927	237,212	756,597	764,652
Purchased gas	147,337	327,132	162,407	63,703	44,574	180,618	451,302	194,827	72,356	51,246	214,174	532,603	572,174
Electric generation fuel	17,584	64,999	13,988	21,014	25,130	20,640	80,772	14,278	19,227	23,807	24,161	81,472	79,239
Residential Exchange	(51,289)	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(54,257)	(35,570)	(34,010)	(51,396)	(175,232)	(175,000)
Unrealized (gain)/loss on derivative instruments	(278)	106	(87)	(2,849)	1,894	516	(526)	0	0	0	0	0	0
Utility operations and maintenance	78,070	289,702	73,855	73,201	67,093	77,083	291,232	76,000	78,000	69,000	78,000	301,000	306,000
Other operations and maintenance	74,900	303,972	67,002	78,545	87,361	89,609	322,517	72,000	81,000	500	500	154,000	2,000
Depreciation and amortization	60,442	236,866	60,288	61,122	62,204	63,228	246,842	62,000	62,500	59,500	61,000	245,000	258,000
Merger and related costs/conservation amort.	9,544	33,458	8,190	4,809	4,747	4,942	22,688	7,000	5,000	5,000	5,000	22,000	22,000
Goodwill Impairment							91,196						
Taxes other than federal income taxes	60,608	208,395	67,492	45,622	46,024	62,843	221,981	69,000	47,000	47,000	64,000	227,000	235,000
Federal income taxes	36,010	72,369	38,711	(2,929)	8,524	30,656	74,962	41,153	9,028	4,374	36,338	90,894	87,547
Total operating expenses	634,855	2,077,628	633,790	480,723	461,126	776,421	2,352,060	690,053	485,947	390,345	668,989	2,235,334	2,151,611
<b>OPERATING INCOME</b>	92,994	305,175	109,680	35,216	53,825	18,031	216,752	112,780	61,699	48,587	105,669	328,736	355,744
<b>OTHER INCOME</b>	(4,050)	1,564	64	1,586	318	2,324	4,292	500	500	500	500	2,000	2,000
<b>INCOME BEFORE INTEREST CHARGES</b>	88,944	306,739	109,744	36,802	54,143	20,355	221,044	113,280	62,199	49,087	106,169	330,736	357,744
<b>INTEREST CHARGES, net of AFUDC</b>	45,483	183,973	43,399	43,270	42,834	43,496	172,999	43,750	45,000	42,750	45,250	176,750	184,000
Mandatorily redeemable securities interest	24	1,072	23	23	23	23	92	23	23	23	23	92	92
Minority interest	71	177	(43)	289	162	(7,477)	(7,069)	150	150	0	0	300	600
Discontinued Operations:													
NET INCOME before effect of acct. change	43,366	121,517	66,365	(6,780)	11,124	(15,687)	55,022	69,357	17,026	6,314	60,896	153,594	173,052
FAS-133 transition adjustment loss (net of tax)		169					0						
Less: Preferred stock dividends/ redemptions	372	5,151					0						
<b>INCOME FOR COMMON STOCK</b>	\$42,994	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$69,357	\$17,026	\$6,314	\$60,896	\$153,594	\$173,052
<b>DILUTED COMMON SHARES OUT. --WEIGHTED</b>	97,228	95,309	99,367	99,371	100,043	99,765	99,911	100,065	100,365	100,665	100,965	100,515	101,715
<b>INCOME FOR COMMON STOCK</b>													
Utility before accounting change	\$43,833	\$113,824	\$66,854	(\$9,634)	\$8,126	\$58,056	\$123,401	\$68,857	\$13,626	\$5,814	\$60,396	\$148,694	\$171,052
Cumulative effect of accounting change		169											
Non-utility	(839)	2,204	(489)	2,854	2,998	(73,743)	(68,379)	500	3,400	500	500	4,900	2,000
Total	\$42,994	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$69,357	\$17,026	\$6,314	\$60,896	\$153,594	\$173,052
<b>EARNINGS PER COMMON SHARE</b>													
Utility	\$0.45	\$1.19	\$0.67	(\$0.10)	\$0.08	\$0.58	\$1.24	\$0.69	\$0.14	\$0.06	\$0.60	\$1.48	\$1.68
Cumulative effect of accounting change		\$0.00											
Non-utility	(0.01)	0.02	(0.00)	0.03	0.03	(0.74)	(0.68)	0.00	0.03	0.00	0.00	0.05	0.02
<b>DILUTED EARNINGS PER SHARE</b>	\$0.44	\$1.22	\$0.67	(\$0.07)	\$0.11	(\$0.16)	\$0.55	\$0.69	\$0.17	\$0.06	\$0.60	\$1.53	\$1.70

\* Company adopted EITF 03-11 on Jan. 1, 2004, which requires most non-trading derivative instruments to be shown net in the income statement. For example, 1Q'03 "sales to other utilities & marketers," a subset of electric revenues, were shown originally as \$57.2 mm, and now are shown as \$21.9 mm. A similar offsetting adjustment was also made to lower purchased electric expenses, leaving net income unchanged. The company has now provided the quarterly reclassifications for 2003.



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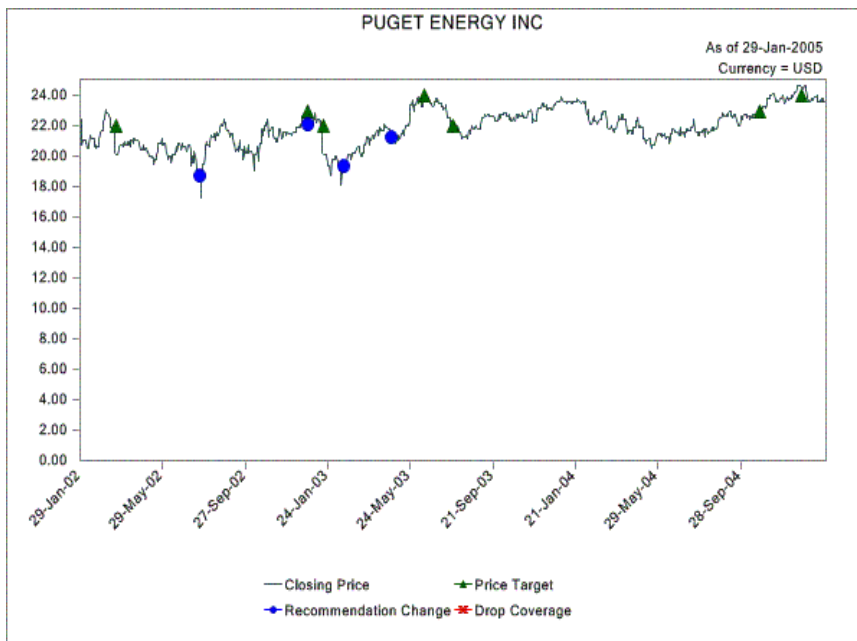
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I, James L. Bellessa, Jr., CFA, attest that (i) all the views expressed in this research report accurately reflect my personal views about the common stock of the subject company, and (ii) no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

### Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 12/31/04)	Buy	Hold	Sell
Corresponding Institutional Research Rating	Buy	Neutral	Underperform
Distribution of Institutional Research Ratings	42%	45%	13%
Corresponding Retail Research Rating	Buy, Core/Buy	Hold, Core/Hold	Avoid
Distribution of Retail Research Ratings	71%	29%	0%
Distribution of combined ratings	47%	42%	11%
Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos	9%	8%	5%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
Strong Buy, Buy, Neutral, Underperform

#### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	27-Dec-2004	24.62	24.00
14-Feb-2003	19.44	BUY	25-Oct-2004	22.71	23.00
26-Dec-2002	22.10	NEUTRAL	24-Jul-2003	22.05	22.00
22-Jul-2002	18.73	BUY	12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00
			21-Mar-2002	20.29	22.00

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

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# UBS Investment Research

## Puget Energy Inc.

### A Mixed Bag

#### ■ Quarter Little Ahead of Estimates

Puget realized a 39% increase in recurring fourth quarter EPS, to \$0.61 from \$0.44 in 4Q03. The results were \$0.02 above our est. of \$0.59 and \$0.05 above consensus of \$0.56. For the year, Puget realized a 34% increase in recurring EPS, to \$1.55 from \$1.16 in 2003.

#### ■ Lowering 2005 and 2006 EPS Estimates

We are lowering our 2005E EPS to \$1.55, from \$1.70, to reflect the earnings lag due to \$400 million of capex at the utility in 2005. The co. has not yet decided on the timing or mechanism of recovery. We also are reducing our 2006 est. to \$1.70, from \$1.85, to reflect the aforementioned earnings lag and likely share dilution to finance the wind acquisitions.

#### ■ Magnitude of Infrastrux Impairment was Disappointing

While welcoming mgmt's strategic decision to sell Infrastrux the size of impairment reduces our expectation of sales proceeds and increases the scale of equity issuance required to finance wind acquisitions.

#### ■ Valuation: See Little Upside

Our 12-mth PT of \$24 (derived using DCF) implies a 14.1x PE on new 2006E EPS, roughly in-line with peers. While new wind generation assets support above average EPS growth at Puget, our view on the stock is tempered by several key risks that the co. faces including regulatory risks, Least Cost Plan execution risks, and high leverage.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,613	2,798	-
EBIT	377	418	436	456	-
Net income (UBS)	110	155	157	172	-
EPS (UBS, US\$)	1.16	1.55	1.55	1.70	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	16.7	16.3	-
ROIC (EBIT) %	-	9.3	9.5	9.9	-
EV/EBITDA x	-	6.9	6.7	6.5	-
PE (UBS) x	-	14.6	15.5	14.1	-
Dividend yield %	-	4.4	4.2	4.2	-

Source: UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$24.00 on 10 Feb 2005

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Electric Utilities

Rating	<b>Neutral 2</b> <i>Unchanged</i>
--------	--------------------------------------

Price target	US\$24.00 <i>Unchanged</i>
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Price	US\$24.00
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RIC: PSD.N BBG: PSD US

11 February 2005

#### Trading data

52-wk. range	US\$24.73-20.54
Market cap.	US\$2.39bn
Shares o/s	99.7m
Free float	80%
Avg. daily volume ('000)	206
Avg. daily value (US\$m)	4.9

#### Balance sheet data 12/05E

Shareholders' equity	US\$1.77bn
P/BV (UBS)	1.3x
Net cash (debt)	(US\$2.60bn)

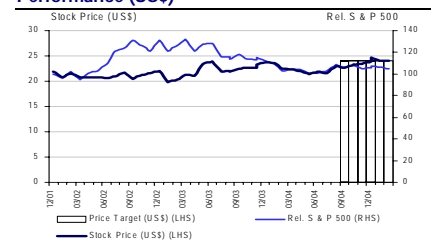
#### Forecast returns

Forecast price appreciation	+0.0%
Forecast dividend yield	4.2%
Forecast stock return	+4.2%
Market return assumption	8.3%
Forecast excess return	-4.1%

#### EPS (UBS, US\$)

	12/05E		12/04	
	From	To	Cons. Actual	
Q1E	-	0.71	0.67	0.67
Q2E	-	0.17	0.17	0.16
Q3E	-	0.09	0.11	0.11
Q4E	-	0.60	0.60	0.61
12/05E	1.70	1.55	1.68	
12/06E	1.85	1.70	1.81	

#### Performance (US\$)



Source: UBS

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#### ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 7

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## Earnings Summary

**4Q04 Review:** Puget realized a 39% increase in recurring fourth quarter diluted EPS, to \$0.61 from \$0.44 in 4Q03. The results were \$0.02 above our estimate of \$0.59 and \$0.05 above the Street consensus estimate of \$0.56. Year-over-year, results were positively impacted by an increase in electric margin due to absence of excess power costs associated with the power cost adjustment (PCA) mechanism, lower income tax expense and higher other income. These positives were partially offset by lower gas volumes due to warmer than normal weather and higher depreciation expense.

**2004 Review:** For the year, Puget realized a 34% increase in recurring diluted EPS, to \$1.55 from \$1.16 in 2003. The results were \$0.05 above our estimate of \$1.50 and \$0.03 above the Street consensus estimate of \$1.52. Year-over-year, results were positively impacted by an increase in electric margin due to absence of excess power costs associated with the PCA mechanism and lower interest expense, partially offset by additional shares outstanding and higher depreciation expense.

Please note, our recurring 2004 EPS excludes a \$0.23 per share disallowance related to the Tenaska project and a \$0.77 per share charge related to the Infrastrux valuation impairment and, hence, differs from the \$0.55 GAAP EPS reported by the company. We would also like to note that our 2003 EPS excludes a \$0.06 per share one-time tax benefit and, hence, differs from the \$1.22 GAAP EPS reported by the company.

**2005 EPS Guidance:** Management intends to issue 2005 EPS guidance after the Washington Utilities and Transportation Commission (WUTC) rules on Puget Sound Energy's (PSE) pending electric and gas case. PSE requested a \$99.8 million and a \$46.2 million rate increase for electric and gas customers, respectively. A ruling is expected no later than March 5, 2005.

**Infrastrux Asset Impairment:** The company completed its strategic review of Infrastrux and has determined that the business no longer fits its core strategy and, hence, intends to monetize the asset. As a result of ongoing challenges in Infrastrux's core business operations, the company took a \$76.6 million non-cash impairment charge in 4Q04, lowering the book value to \$33.4 million from \$110 million.

**Wind Update:** Management provided an update with respect to the two recently announced wind power projects – the 150 MW Hopkins Ridge project and the 160 MW Wild Horse project. The Hopkins Ridge project has been expeditiously reviewed and permits are pending. The Bonneville Power Administration (BPA) has facilitated transmission service to this project allowing for a December 2005 on-line target date. The Wild Horse project will likely be completed by the end of 2006; progress in the permitting process has

also been made and the plant is expected to use the existing PSE transmission once it comes on-line.

## Our View

Our reaction to Puget's quarterly results is a bit mixed. Earnings came in slightly better than expected, no doubt aided by the strong electric retail sales trend the utility is experiencing on the back of regional economic strength. The decision to sell Infrastrux was also welcome news given the onerous cash requirements at the utility. However, we were disappointed by the size of the impairment charge that Infrastrux had to take, which greatly reduces our expectation of what that business could be sold for. Thus we believe an equity issuance to finance the wind acquisition is more probable and imminent than our earlier expectation. Another disappointment was the revelation in the conference call that the utility faces an earnings lag in recovering its capital investments in 2005. The company has not yet decided on the timing or the mechanism of the cost recovery, but this only adds to a plethora of regulatory issues that are either pending or forthcoming at the utility.

While the addition of new generation assets to rate-base supports our thesis of above average earnings growth at Puget over the intermediate term, our view on the stock is somewhat tempered by several key risks that face the company, including the possibility of an unfavorable rate case decision, Least Cost Plan execution risks, and still high leverage (leverage fell to 60% at the end of 2004).

## Lowering 2005 and 2006 EPS Estimates

We are lowering our recurring 2005 EPS estimate to \$1.55, from \$1.70, to reflect the earnings lag resulting from the impact of \$400 million of capex at the utility in 2005 (which in itself is higher than our initial \$345 million capex estimate). PSE will need to file with the WUTC to recover the costs associated with this capital investment. The company has not decided on the timing or mechanism of recovery, hence, introducing an earnings lag of \$0.15 per share. Out of this, \$0.10 is attributable to higher depreciation and \$0.05 to higher O&M. Please note, the outcome of the pending general rate case, sale of Infrastrux, and mode of financing of wind projects (possible share dilution if equity issuance completed in 2005) could materially affect our 2005 estimates. The Street consensus for 2005 is \$1.68 (reflecting a range of \$1.50 – 1.83).

We are also lowering our 2006 EPS estimate to \$1.70, from \$1.85, to account for the aforementioned earnings lag resulting from the 2005 capex and share dilution resulting from our expectation that Puget will need to issue equity to finance the wind projects. Again, our estimates could be impacted by the timing of cost recovery and the actual size of a potential equity offering. The Street consensus estimate for 2006 currently stands at \$1.81, reflecting a range of \$1.70 – 1.89.

## Valuation

Our 12-month price target of \$24 per share is derived using a DCF analysis. This implies a 14.1x PE on our recurring 2006 EPS or in-line with peers. Price movement to \$24 per share – when combined with the current \$1.00/share annual dividend (or 4.2% yield) – suggests a 4.2% total return potential.

## Key 4Q04 Drivers

**Puget Sound Energy (PSE)**, the utility, realized a 34% increase in fourth quarter recurring EPS, to \$0.59 from \$0.44 in 4Q03. The increase was led by higher electric margins, which includes the electric rate tariff increase, effective May 2004, to reflect the Frederickson acquisition (\$0.08). Other positives include lower income tax expense (\$0.05) and lower interest expense (\$0.02). The non-regulated business at the utility benefited from gains on property sales (\$0.06). These positives were partially offset by a decrease in gas margin primarily due to warmer than normal weather (\$0.02), higher depreciation expense (\$0.02), the impact of share dilution (\$0.01), and other (\$0.01).

Electric retail sales were roughly flat quarter-over-quarter despite a 2.4% increase in customers. This was led by 0.6% and 0.5% increase in commercial and industrial sales, respectively, offset by a 0.2% decline in residential sales. Gas volumes declined 4.3%, led by a 6% decline in residential volumes. Commercial and transportation volumes also fell 3.1% and 2.6%, respectively. The only bright spot was a 5.4% increase in industrial volumes but this was not enough to offset the large decline in residential volumes. The quarter-over-quarter decline in gas volumes can be partially explained by 3% warmer weather versus the year-ago quarter. On the positive side, new accounts grew 4.1% compared with 4Q03.

**Infrastrux** realized a 100% increase in recurring 4Q diluted EPS, to \$0.02 from \$0.01 in 3Q03. Infrastrux benefited from a 20% revenue increase over the year-ago quarter.

## Key 2004 Drivers

**Puget Sound Energy (PSE)**, the utility, realized a 28% increase in recurring diluted EPS, to \$1.49 from \$1.16 in 2003. The increase was led by an increase in electric margin in 2004 (\$0.23) due to PSE hitting the cap for the PCA mechanism in 2004. Electric margins were also positively impacted by \$0.04 due to a rate increase in May 2004 for Frederickson plant addition. Other positive impacts included lower interest expense and absence of the preferred stock dividend (\$0.14), the absence of the venture capital impairment (\$0.04) and lower income tax expense (\$0.03). These positives were partially offset by additional shares outstanding (\$0.06), higher depreciation expense (\$0.06), other (\$0.02), and lower gas margin (\$0.01).

Electric retail sales increased 1.5% due to strong electric customer growth of 2.2%. Commercial and residential sales increased 2.8% and 1.9%, respectively. Industrial sales declined 1.5% year-over-year. PSE continued to experience strong gas customer growth of 3.7%, however, gas volumes declined 1.5% primarily due to warmer than normal weather in 2004. The decline in gas volumes was led by lower transportation and residential volumes of 3.7% and 2.2%, respectively, partially offset by an increase of 4.0% and 0.7% in industrial and commercial volumes, respectively. In 2004, weather was 8% warmer than normal and 2% warmer than 2003.

**Infrastrux** realized recurring 2004 diluted EPS of \$0.06, up from \$0.02 in 2003. These results exclude the impact of the \$77.6 million impairment recorded in 4Q04, to reflect the ongoing challenges in the utility construction services sector.

## ■ Puget Energy Inc.

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. InfrastruX provides infrastructure construction services to the electric and gas utility industries.

## ■ Statement of Risk

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. The utility has recently filed a general electric and gas rate case to request a \$128 million rate increase. However, the WUTC might not award the entire rate increase. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.



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UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	36%	32%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	53%	35%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	29%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 31 December 2004.

#### KEY DEFINITIONS

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

**Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

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**US Closed-End Fund ratings and definitions are:** Buy: Higher stability of principal and higher stability of dividends; Neutral: Potential loss of principal, stability of dividend; Reduce: High potential for loss of principal and dividend risk.

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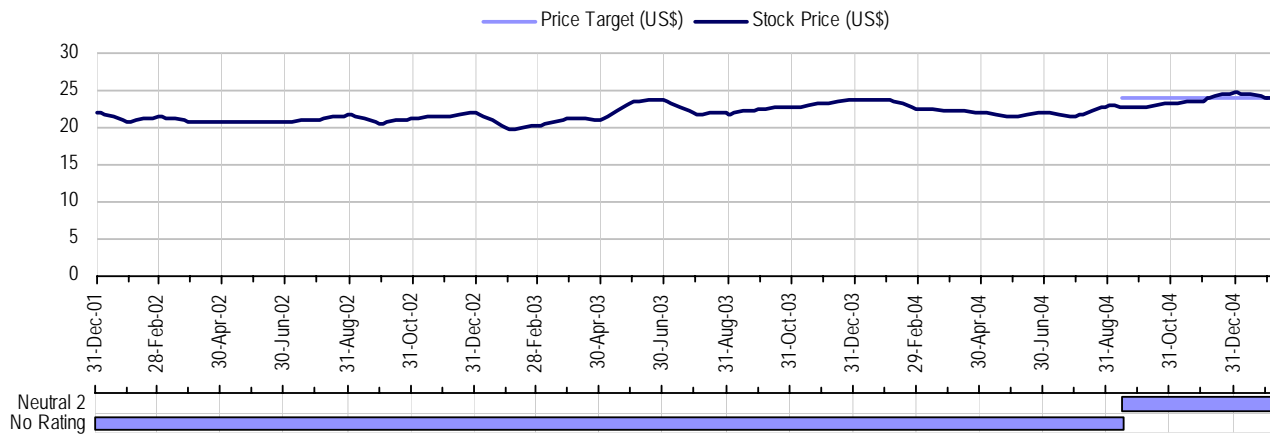
#### Companies mentioned

Company Name	Reuters	Rating	Price
<b>Puget Energy Inc.</b> <sup>4,5,6a,6b,6c,7,16</sup>	PSD.N	Neutral 2	US\$24.00

Price(s) as of 10 February 2005. Source: UBS.

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**Puget Energy Inc. (US\$)**



Source: UBS; as of 10 February 2005.

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11 February 2005

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# Puget Energy Inc.

**Testing the Regulatory Compact**
**NEUTRAL**
**Reason for Report:** Q4 and Year end earnings

**Volatility Risk:**  
**MEDIUM**
**Price: \$24.00**

Estimates (Dec)	2004A	2005E	2006E
EPS:	\$1.60	\$1.68	NA
P/E:	15.0x	14.3x	NM
GAAP EPS:	\$0.55	\$1.68	NA
GAAP P/E:	43.6x	14.3x	NM
EPS Change (YoY):		5.0%	NM
Cash Flow/Share:	NA	NA	NA
Price/Cash Flow:	NM	NM	NM
Dividend Rate:	\$1.00	\$1.00	\$1.00
Dividend Yield:	4.2%	4.2%	4.2%

**Opinion & Financial Data**

Investment Opinion:	B-2-7
Mkt. Value / Shares Outstanding (mn):	\$2,328 / 97
Book Value/Share (Mmm-yyyy):	NA
Price/Book Ratio:	NM
Total Debt / Capital:	54.1%
Est. 5 Year EPS Growth:	8.0%
Est. 5 Year Dividend Growth:	0.0%

**Stock Data**

52-Week Range:	\$24.81-\$20.51
Symbol / Exchange:	PSD / New York
Institutional Ownership-Vickers:	47.6%

**Highlights:**

- Decent Numbers.** PSD reported earnings of \$0.55 for year-end vs. \$1.22 in 2003. Q4 earnings came in at a loss of \$0.16 vs. \$0.44 for Q403. Recurring EPS for the year was \$1.60, excluding a \$0.77 non-cash impairment charge (after tax) for Infrastrux and a regulatory disallowance (after tax) of \$0.28. Recurring 2003 EPS was \$1.26.
- Sayonara, Infrastrux.** PSD has decided to monetize this as it no longer fits the core integrated utility strategy. This segment reported a loss of \$0.70 for the year, including a \$0.77 after tax impairment charge. Excluding this charge, recurring EPS was \$0.06, \$0.04 above 2003 EPS of \$0.02.
- Rate Wait.** PSD won't provide 2005 EPS guidance until it receives a final rate order from the Washington Utilities Commission; that's expected by early March. PSD has asked for an electric rate increase of 7.1%, \$99.8 million and 6.3% natural gas increase of \$46.2 million, totaling \$146 million.
- Buy Now, Get Paid Later.** A rate hike will certainly help, but the Q4 earnings release and conference call suggest that PSD will be back again soon, and not just to address adding new wind power resources to the rate base. Capex this year is expected in the \$600M range, only \$200M of which is for generation. DD&A and O&M expense will be pressured as these facilities are built but not yet included in rates.
- More Shares?** Financing capex of this magnitude—and meeting the stated goal of improving the balance sheet—likely means further equity financing. We estimate 2005 operating cash at \$470, the dividend takes just under \$100M, leaving a \$200M+ shortfall.
- Regulatory Backdrop?** PSD is doing the right things, and shares appear fairly valued. Regulatory climate—which is presently in flux—will clearly be a key driver for the next several years.

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## More on Q4 / 2004 Results

Utility (PSE) GAAP earnings came in at \$1.26 vs. \$1.20 in 2003. Recurring EPS for PSE in 2004 was \$1.54, which excludes a \$0.28 disallowance charge, and up \$0.30/sh from recurring 2003 EPS of \$1.24. PSE earnings were driven by an increase in electric margin, lower interest expense and preferred stock dividends, and an increase in other income.

Electric margins were higher in 2004, primarily because of stronger retail sales and a rate increase received last May. The rate increase of \$44M on an annualized basis, essentially allows PSD to recover higher power costs incurred, including the 50% investment in the Frederickson power plant.

In addition to approving the rate increase, the WUTC also issued a separate order last May disallowing certain fuel costs associated with the Tenaska generating facility. PSD wrote-off \$0.28/share in association with the Tenaska disallowance last year, and anticipates another \$0.07/share this year. Management will provide more details when it announces its 2005 earnings guidance.

Weather for the year was 8% warmer than normal and 2% warmer than last year. Hydro declined and has been below normal in the Pacific Northwest for the last five of six years. While weather clearly impacted both electric and gas earnings negatively, power costs associated with the poor hydro conditions will not impact earnings as they are recoverable through a PCA balancing mechanism.

## Regulatory Matters

PSD has not yet provided guidance for 2005, and won't until it receives a final order on the pending electric and gas rate cases from Washington Utilities and Transportation Commission. That is expected early next month.. PSD has asked for an electric rate increase of 7.1%, \$99.8 million and 6.3% natural gas increase of \$46.2 million, totaling \$146 million. As noted previously, the request would add close to \$40M of net income, or about \$0.40 per share. Our current 2005 outlook factors in a modest 2005 benefit, reflecting a portion of the request implemented after the busy first quarter. Our full-year rate increase assumption is around half of the original request.

### ■ Changing Landscape

PSD is anticipating some political and regulatory changes in its home state. After a protracted and challenged election, a new Democratic governor has taken office, which raises questions about appointments to various state agencies, including the WUTC. One member of the three-person panel has already retired, and the future of the others remains up in the air. We've found incumbent Chair Marilyn Showalter to be thoughtful, balanced, and cognizant of investor and consumer issues. Whether she remains at the Commission remains unclear, although she will preside over PSD's currently pending rate cases.

More positively, PSD anticipates a settlement agreement to give the utility a new Baker River Hydro license for at least 45 years. This would allow PSD to maintain low cost hydropower to customers. They are also looking to acquire some wind facilities, including the Hopkins Ridge and Wild Horse wind projects to provide energy to customers and protect them from volatile energy prices adding about 380 megawatts of wind energy.

## Outlook

Absent any clarification on the rate outcome, we are maintaining our 2005 estimate of \$1.68 and as noted are including a portion of the rate request in our 2005 estimate of \$1.68/sh. We also exclude InfrastruX. Currently, shares of PSD are trading at 14.3x our 2005 estimate, between the LDC and electric utility averages. At that level, a decent regulatory outcome is assumed.

### ■ The Regulatory Direction is Key

Longer term, we note that Puget's hearty capex budget over the next several years will likely keep the company not only in front of regulators, but Wall Street as well. That budget reflects the need to invest; not only to keep pace with customer growth but also to continue weaning the region from its dependence on increasingly fickle hydroelectric power. At PSD, operating cash flow alone isn't sufficient to fund this initiative; ergo, additional new external financing will almost surely be needed.

The newly elected and appointed officials in Olympia face a challenge. Energy costs are rising nationwide, a burden that is already showing up in customer bills. At the same time, the region's growing economy depends in large part on a stable, dependable, environmentally responsible, and economically viable portfolio of energy resources, a goal inextricably tied to ongoing further development of associated energy infrastructure.

The state's two major utilities, PSD and its eastern neighbor Avista, are taking steps to meet that challenge by committing substantial capital to investments that should be attractive over time to their share and bond holders. The question is whether the utilities—and specifically their investors--will be compensated in a manner sufficient to continue attracting needed capital.

Despite some bumps in the road, over the past couple of years we've sensed a constructive tenor on this issue at the top echelons of the WUTC, if not consistently at the Staff level. With the direction of that critical agency presently at a crossroads, we maintain our Neutral stance on Washington utility stocks.

**Table 1: Recurring EPS 2004A vs 2003A**

	PSE	InfrastruX	Consolidated
2004			
Reported EPS	1.26	(0.71)	0.55
Non recurring Items	0.28	0.77	1.05
Recurring EPS	1.54	0.06	1.60
2003			
Reported EPS	1.20	0.02	1.22
Non recurring Items	0.04	---	0.04
Recurring EPS	1.24	0.02	1.26

Source: ML Estimates, Company reports

**Table 2: PSD 2004A-2005E**

Consolidated Income Statement	2004A	2005E
Operating Revenues		
Electricity	\$1,423.0	\$1,488.7
Gas	769.3	797.0
Non-Utility Construction Services		
Other	376.5	357.0
Total	\$2,568.8	\$2,642.7
Cost of Energy		
Purchased Electricity	\$723.6	\$738.0
Purchased Gas	408.5	423.2
Electric Gen Fuel	80.8	84.5
Unrealized (gain) loss on derivative instruments	(0.5)	---
Res. Exchange	(174.5)	(175.0)
Total Cost of Energy	\$1,037.8	\$1,070.7
Gross Margin	\$1,531.0	\$1,571.9
Operating Expenses		
Utility O&M	\$291.2	\$301.2
Other O&M	322.5	332.0
DD&A	246.8	248.1
Conservation Amort	22.7	23.0
Other Taxes	222.0	228.4
Other	---	---
Total	\$1,105.3	\$1,132.7
Operating Income	\$425.7	\$439.3
Interest Expense	173.1	167.8
AFUDC	---	---
Minority Interest	7.1	7.0
Other Income		
Other Income	4.3	3.0
Income Before Income Taxes	\$249.8	\$267.5
Income Taxes	90.2	96.3
Income from Continuing Ops	\$159.7	\$171.2
Preferred Dividends	---	---
Operating Net to Common	\$159.7	\$171.2
Non-Recurring Items	(104.8)	---
Reported Net to Common	\$54.9	\$171.2
Avg. F-D Shares Outstanding		
Avg. F-D Shares Outstanding	99.9	101.9
Operating EPS		
Operating EPS	\$1.60	\$1.68
Non-Recurring Items	(\$1.05)	---
Reported EPS	\$0.55	\$1.68

Source: Merrill Lynch & Company Reports

### Analyst Certification

I, Sam Brothwell, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.



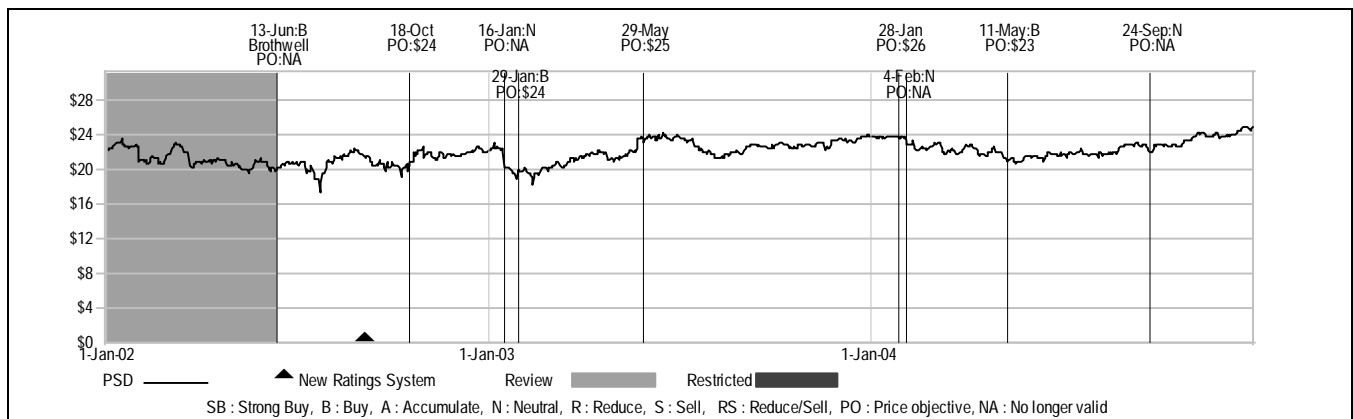
**Puget Energy**  
**4Q'04 Earnings Summary**  
(\$MM, except where noted)

<b>Consolidated Income Statement</b>	<b>4Q'04</b>	<b>4Q'03</b>	<b>Change</b>	<b>% Change</b>	<b>Segment Detail</b>	<b>4Q'04</b>	<b>4Q'03</b>	<b>Change</b>	<b>% Change</b>
<b>Operating Revenues</b>					<b>Revenues</b>				
Electricity	\$404.8	\$386.5	\$18.3	5%	<b>Electric</b>				
Gas	284.7	251.5	33.2	13%	Residential	\$169.8	\$165.1	\$4.7	3%
Non-Utility Construction Services	---	---	---	n/m	Commercial	152.1	147.8	4.3	3%
Other	105.0	89.8	15.2	17%	Industrial	23.5	23.0	0.5	2%
Total	\$794.5	\$727.8	\$66.6	9%	Sub-Total	\$345.4	\$335.8	\$9.6	3%
<b>Cost of Energy</b>					Other retail sales	23.5	24.1	(0.6)	-3%
Purchased Electricity	\$205.8	\$201.9	\$3.8	2%	Transportation and Marketers & Other	3.4	2.3	1.1	45%
Purchased Gas	180.6	147.3	33.3	23%		32.5	24.3	8.3	34%
Electric Gen Fuel	20.6	17.6	3.1	17%	Total Electric	\$404.8	\$386.5	\$18.3	5%
Unrealized (gain) loss on derivative instruments	0.5	(0.3)	0.8	n/m	<b>Gas</b>				
Res. Exchange	(50.7)	(51.3)	0.6	1%	Residential	\$183.6	\$165.5	\$18.1	11%
Total Cost of Energy	\$356.9	\$315.3	\$41.6	13%	Commercial	81.6	70.0	11.6	17%
<b>Gross Margin</b>	<b>\$437.6</b>	<b>\$412.6</b>	<b>\$25.0</b>	<b>6%</b>	Industrial	13.4	10.6	2.8	26%
<b>Operating Expenses</b>					Transportation	3.3	3.3	(0.0)	-0%
Utility O&M	\$77.1	\$78.1	(\$1.0)	-1%	Other	2.8	2.6	0.2	7%
Other O&M	89.6	74.9	14.7	20%	Total Gas	\$284.6	\$252.0	\$32.6	13%
DD&A	63.2	60.4	2.8	5%	<b>Total Energy Revenues</b>	<b>\$689.4</b>	<b>\$638.5</b>	<b>\$50.9</b>	<b>8%</b>
Conservation Amort	4.9	9.5	(4.6)	-48%	<b>Volumes</b>				
Other Taxes	62.8	60.6	2.2	4%	<b>Electricity (gWh)</b>				
Other	---	---	---	n/m	Residential	2,660.2	2,665.6	(5.3)	-0%
Total	\$297.7	\$283.6	\$14.1	5%	Commercial	2,133.8	2,121.6	12.2	1%
<b>Operating Income</b>	<b>\$139.9</b>	<b>\$129.0</b>	<b>\$10.9</b>	<b>8%</b>	Industrial	344.2	342.6	1.6	0%
Interest Expense	43.5	45.5	(2.0)	-4%	Sub-Total	5,138.3	5,129.8	8.5	0%
AFUDC	---	---	---	n/m	Sales for resale	386.8	425.4	(38.5)	-9%
Minority Interest	7.5	0.1	7.4	10,431%	Transportation	515.3	499.2	16.2	3%
Other Income	2.3	(4.1)	6.4	n/m	Other	323.6	345.1	(21.5)	-6%
Income Before Income Taxes	\$91.2	\$79.4	\$11.8	15%	Total Electric	6,364.1	6,399.4	(35.4)	-1%
Income Taxes	30.7	36.0	(5.4)	-15%	<b>Gas (MMBtu)</b>				
Income from Continuing Ops	\$60.6	\$43.4	\$17.2	40%	Residential	173.9	185.1	(11.2)	-6%
Preferred Dividends	---	0.4	(0.4)	-100%	Commercial	87.6	90.4	(2.8)	-3%
<b>Operating Net to Common</b>	<b>\$60.6</b>	<b>\$43.0</b>	<b>\$17.6</b>	<b>41%</b>	Industrial	15.1	14.3	0.8	5%
<b>Non-Recurring Items</b>	<b>(76.6)</b>	<b>(76.6)</b>	<b>n/m</b>	<b>n/m</b>	Transportation	52.8	54.2	(1.4)	-3%
<b>Reported Net to Common</b>	<b>(\$16.0)</b>	<b>\$43.0</b>	<b>(\$59.0)</b>	<b>n/m</b>	Total Gas	329.3	344.0	(14.6)	-4%
Avg. F-D Shares Outstanding	99.8	97.2	2.5	3%	<b>Revenue Per Unit</b>				
<b>Operating EPS</b>	<b>\$0.61</b>	<b>\$0.44</b>	<b>\$0.17</b>	<b>38%</b>	<b>Electricity (\$/kWh)</b>				
<b>Non-Recurring Items</b>	<b>(\$0.77)</b>	<b>---</b>	<b>(\$0.77)</b>	<b>n/m</b>	Residential	\$0.064	\$0.062	\$0.00	3%
<b>Reported EPS</b>	<b>(\$0.16)</b>	<b>\$0.44</b>	<b>(\$0.60)</b>	<b>n/m</b>	Commercial	0.071	0.070	0.00	2%
Tax Rate	34.5%	43.2%			Industrial	0.068	0.067	0.00	2%
<b>Heating Degree Days</b>	<b>1,642</b>	<b>1,695</b>	<b>(53)</b>	<b>-3%</b>	Sub-Total	\$0.067	\$0.065	\$0.00	3%
% of Normal	95%	98%			Sales for resale	0.061	0.057	0.00	7%
<b>Customers</b>					Other	0.043	0.031	0.01	36%
Electric	999	976	23	2%	Total Electric	\$0.064	\$0.060	\$0.00	5%
Natural Gas	668	642	26	4%	<b>Electricity Cost (\$/kWh)</b>	\$0.032	\$0.032	\$0.00	2%
Book Value	15.60	15.34			<b>Electricity Gross Margin</b>				
					Residential	\$0.032	\$0.030	\$0.00	4%
					Commercial	0.039	0.038	0.00	2%
					Industrial	0.036	0.036	0.00	1%
					Sub-Total	\$0.035	\$0.034	\$0.00	3%
					Sales for resale	0.028	0.025	0.00	13%
					Other	0.010	(0.000)	0.01	n/m
					Total Electric	\$0.031	\$0.029	\$0.00	8%
					<b>Gas (\$/MMBtu)</b>				
					Residential	\$10.56	\$8.94	\$1.61	18%
					Commercial	9.32	7.75	1.57	20%
					Industrial	8.87	7.39	1.47	20%
					Transportation	0.62	0.61	0.02	3%
					Total Gas	\$8.64	\$7.33	\$1.32	18%
					<b>Gas Cost</b>	<b>\$5.48</b>	<b>\$4.28</b>	<b>\$1.20</b>	<b>28%</b>
					<b>Gas Gross Margin</b>				
					Residential	\$5.07	\$4.66	\$0.41	9%
					Commercial	3.83	3.46	0.37	11%
					Industrial	3.38	3.11	0.27	9%
					Transportation	0.62	0.61	0.02	3%
					Total Gas	\$3.16	\$3.04	\$0.12	4%



## Important Disclosures

PSD Price Chart



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Investment Rating Distribution: Energy Group (as of 31 December 2004)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	47.06%	Buy	28	38.89%
Neutral	76	49.67%	Neutral	29	38.16%
Sell	5	3.27%	Sell	0	0.00%
Investment Rating Distribution: Global Group (as of 31 December 2004)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1054	40.45%	Buy	383	36.34%
Neutral	1339	51.38%	Neutral	382	28.53%
Sell	213	8.17%	Sell	43	20.19%

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# Puget Energy, Inc.

## PSD Positions InfrastruX for Sale, Excluding Charges Q4 Slightly Above Expectations, Maintain Market Outperform

### Investment Summary

PSD reported fourth quarter results of a loss of \$0.16 compared to \$0.44 the prior year and below our \$0.57 estimate. Excluding a \$0.77 charge for writing down its InfrastruX division, the Company reported \$0.61 or slightly ahead of our estimate. The write-down indicates the Company is serious about disposing of InfrastruX and returning to a vertically integrated utility. We are lowering FY'05 to \$1.36 (which does not include any rate increases from its upcoming rate case) from \$1.50. In addition, we are initiating a FY'06 estimate of \$1.50. We are maintaining our Market Outperform rating and our target price of \$25.

- PSD reported an increase of \$12.2 million in electric margins mainly due to rate increases and lower power costs. Gas margins declined \$3.5 million mainly due to unfavorable weather and lower consumption by customers as result of higher natural gas prices. Heating degree days were 5% lower than normal due to warmer weather and 3% lower than last year. Growth in the Northwest continued as its customer base increased 2.3% on the electric side and 4.1% on the natural gas side.
- The Company recorded a goodwill impairment charge of \$91 million (pre-tax) or \$0.77 (after-tax) in its InfrastruX division. PSD also expressed an intention to sell this division. We view this as positive, since after the sale, all the operations would be regulated.
- Puget Sound Energy is also expecting to hear a final decision on its pending rate cases by March 5, 2005. The Company has not issued any guidance for FY'05 pending this decision. The staff has recommended \$21.4 million in the electric case compared to the requested \$99.8 million and \$8.1 million in the gas case compared to the requested \$46.2 million. Our estimates do not include the outcome of this case.

### Valuation

Currently, the stock is trading at 17.5x our FY'05 estimate of \$1.36 and 15.8x our FY'05 estimate of \$1.50, which is slightly at a premium to the peer group. It is selling at a slight discount with the peer group on an Enterprise Value to EBITDA basis and Price to Book basis. We are leaving our target price of \$25 unchanged, which is 15.5x (compared to peer group average of 15x) our FY'05 estimate plus a conservative estimate of \$0.25 from the rate case. Given that our estimates are conservative, we are maintaining our Market Outperform rating.

### Regional Growth February 15, 2005

**Puget Energy Inc**  
**PSD/NYSE**  
**Intraday Price on 2/15/05: \$23.77**  
**12-Month Price Target: \$25.00**  
**Market Outperform**

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52-Week Range	\$20.51 – \$24.81
Average Daily Volume	268,488
Shares Outstanding	99.8 million
Market Capitalization	\$2,372 million
Market Cap./2005E Revenue	1.04x
Long Term Debt (Mil)	\$2,097
Total Debt / Total Capitalization	53%
Institutional Ownership	48%
Trailing 12 mo. Revenue	\$2,569 million
Book Value per Share (09/04)	\$16.67
Tangible Book Value/Share (09/04)	\$15.16
Long-Term Projected EPS Growth	5%
Dividend	\$1.00
Dividend Yield	4.2%

#### Annual Estimates

FY (Dec)	2003A	2004A	2005E	2006E
Revs (Mil)	\$2,492	\$2,539	\$2,273 <sup>®</sup>	\$2,342
% chg y/y	4%	2%	(12%)	3%
<b>EPS</b>	<b>\$1.22</b>	<b>\$0.55<sup>+</sup></b>	<b>\$1.36<sup>®</sup></b>	<b>\$1.50</b>
Street	-	-	\$1.63	\$1.78
Price/EPS	19.5x	NMF	17.5x	15.8x

#### Quarterly EPS Estimates

FY (Dec)	Mar	Jun	Sep	Dec
2005E	\$0.60	\$0.09	\$0.06	\$0.62
Street	\$0.68	\$0.17	\$0.07	\$0.60
2004A	\$0.67	(\$0.07)*	\$0.11	(\$0.16) <sup>+</sup>
2003A	\$0.45	\$0.22	\$0.10	\$0.45

\*Includes a \$0.28 charge related to Tenaska Order

<sup>+</sup>Includes a \$0.77 charge related to goodwill impairment

<sup>®</sup>Excludes InfrastruX's operations

**Required Disclosures: C-2**  
**See Page 4 for Required Disclosures**

**See Page 5 for Risks to Price Target**

### Equity Research

1125 17th Street  
 Suite 1600  
 Denver, CO 80202  
 800-525-9899

**Fourth Quarter Highlights**

PSD reported a fourth quarter loss of \$0.16 compared to \$0.44 the prior year. Excluding a \$0.77 charge for goodwill impairment in the Company's InfrastruX division, the Company reported \$0.61 versus our estimate of \$0.57. The increase in earnings was due to an increase in electric margins. Electric margins increased \$12.2 million as a result of increased rates related to the Frederickson plant acquisition and lower excess power costs. Margins from the gas distribution decreased \$3.5 million due to warmer temperatures and lower customer usage, which resulted from higher gas prices. Heating degree days were 5% lower than normal and 3% below Q4'03. Customer growth in the electricity division was 2.3% and 4.1% in natural gas division. InfrastruX, the unregulated segment, reported Q4 net income of \$1.9 million or \$0.02 prior to the charge up from \$0.07 million or \$0.01 in Q4'03. Including the charge, InfrastruX had a loss of \$0.75. Interest expense declined 4% to \$43.5 million due to refinancing at lower rates. Income tax expenses declined 15% to \$30.7 million from \$36.0 million while the tax rate declined slightly to 40.5% from 43.1% the prior year. The net loss of \$15.6 million included an after tax charge of \$76.6 million. Excluding the charge, the Company had after tax net income of \$60.9 million compared to \$ 43.0 million the prior year.

**InfrastruX**

The Company has decided to sell InfrastruX as it is not seen as core for the Company. The Company took a non-cash charge of \$91 million (pretax) to write down the goodwill associated with all the acquisitions it had done in building InfrastruX. For the year, InfrastruX had sales of \$370 million and produced EBITDA of \$36 million. InfrastruX has debt of \$160 million associated with it and assuming a 6-8 multiple would imply an equity value of \$56 to \$128 million. We would anticipate the Company to reduce debt with the net proceeds pending any other uses.

**Balance Sheet**

Total Long-Term Debt at the end of December was \$2.1 billion or 53% of the total capital. The Company incurred approximately \$400 million in cap ex in 2004. PSD guided that its cap ex for 2005 will be approximately \$600 million roughly \$200 million of which will be used on wind power projects.

**Outlook**

The Company has not provided guidance pending the rate case decision which is expected in March 2005. Currently, the staff has recommended \$21.4 in the electric rate case compared to the requested \$99.8 million and \$8.1 million in the gas rate case compared to the requested \$46.2 million. This gives a range of \$29.5 million to \$146 million in total within which the Commission could approve an increase.

We have lowered our FY'05 estimate to \$1.36 from \$1.50 due to certain additional O&M and D&A charges. We would like to remind investors that our estimates do not include any effect of the pending rate cases. We have also not considered any contribution or charges from InfrastruX in our estimates. We are projecting revenues of \$2.3 billion for FY'05, approximately, 3% increase over FY'04 revenues on a comparable basis (excluding InfrastruX). Gross margin (revenue less energy costs) is estimated to increase roughly 6% to \$1.2 billion compared to \$1.1 billion (excluding InfrastruX) in FY'2004. Net income is projected to increase to \$136.8 million compared to \$126.2 million (utility earnings in 2004 including Tenaska disallowances) in FY'04 on normal growth assumptions, lower Tenaska charges. EPS is estimated to increase to \$1.36 from \$1.26 (utility earnings in 2004 including Tenaska disallowances) on roughly 5% more shares.

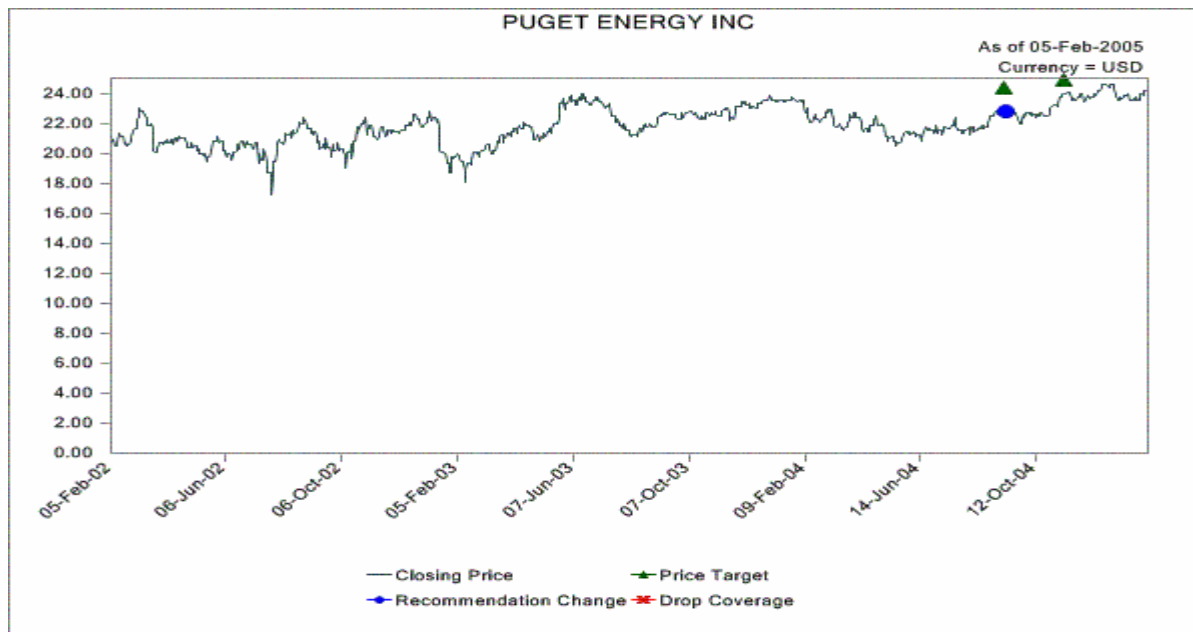
For FY '06, we are estimating revenues of \$2.3 billion or 3% higher than our FY'05 estimate. Gross margin is estimated to increase 4% to \$1.2 billion. Net income is projected to increase 10% to \$150.7 million compared to FY'05 net income of \$136.8 million. EPS is expected to be \$1.50 based on roughly 1% more shares.

**Valuation**

Our FY'05 estimate does not include any effect of the pending rate cases. Taking a conservative approach, we estimate that the rate case could add \$0.25 to FY'05 earnings, which would result in FY'05 EPS of \$1.61. We are leaving our target price of \$25 unchanged, which is 15.5x (compared to peer group average of 15x) our FY'05 estimate plus a conservative \$0.25 from the rate case. Given that the Company is selling its non-regulated business, in our opinion, the risk profile should improve as all the income would be from regulated business. Therefore, we believe the Company could be assigned higher multiples than the peer group. However, pending a decision of the rate case, we are leaving our target price unchanged until more details are disclosed in March 2005. We are maintaining our Market Outperform rating.



**EFFECTIVE NOVEMBER 13, 2002, STIFEL NICOLAUS ELIMINATED PRICE TARGETS ON ALL MARKET PERFORM-RATED STOCKS. ALL MARKET OUTPERFORM AND MARKET UNDERPERFORM-RATED STOCKS CONTINUE TO HAVE PRICE TARGETS.**



**PUGET ENERGY INC**

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
09-Sep-2004	22.88	MARKET OUTPERFORM	08-Nov-2004	24.05	25.00
			09-Sep-2004	22.88	24.50

*We, the research analysts responsible for this report, attest that the views expressed in this research report accurately reflect our personal views about any and all of the subject securities or issuers. We have not received, and will not receive, compensation in return for the specific recommendations or views expressed by us in this report.*

KEY FOR DISCLOSURES: A – Stifel, Nicolaus makes a market in the common stock of this company. B – The analyst owns the common stock of this company. B-1 – A member of the analyst’s household owns the common stock of this company. C – Stifel, Nicolaus has managed or co-managed a public offering of securities for this company within the past 12 months. C-1 – Stifel, Nicolaus has been compensated for investment banking services by this company within the past 12 months. C-2 – Stifel, Nicolaus intends to seek compensation for investment banking services from this company in the next 3 months. D – The analyst serves on the Board of Directors of this company. D-1 – A member of the analyst’s household serves on the Board of Directors of this company. E – Stifel, Nicolaus beneficially owns in excess of 1% of a class of common equity securities of this company.

RATING SYSTEM: Market Outperform – The total return of the stock, adjusted for risk, is expected to outperform the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Perform – The total return of the stock is expected to perform in line with the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Underperform – The total return of the stock is expected to Underperform the broad U.S. equity market, defined as the Russell 2000, over the next 12 months. The security should be sold if such sale is consistent with clients' needs and objectives. Our 12-month price targets may temporarily vary from these expectations due to market volatility.

RESEARCH COVERAGE: As of December 31, 2004 Stifel Nicolaus had 229 companies under coverage. Stifel Nicolaus rated 119 companies, or 52%, as Market Outperform/“Buy,” 105 companies, or 46%, as Market Perform/“Hold,” and 5 companies, or 2%, at Market Underperform/“Sell.” During the previous 12 months, Stifel Nicolaus provided investment banking services for 22 of the companies rated Market Outperform/“Buy” (18%), 17 of the companies rated Market Perform/“Hold” (16%), and none of the companies rated Market Underperform/“Sell” (0%).

The information and statistical data contained herein have been obtained from sources we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to any changes in figures or our views.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST. Please contact the analyst for further information. Stifel, Nicolaus & Company, Inc. research is also available online at [www.multex.com](http://www.multex.com) and [www.firstcall.com](http://www.firstcall.com).

This is not a solicitation of any order to buy or sell.

**Risks to Price Target:**

**Specific risks to our price target include 1) unanticipated unfavorable decision or less than estimated accretion from the pending rate case 2) unanticipated unfavorable weather and 3) unanticipated additional losses or charges relating to divestiture of InfrastruX.**

**Price Target Valuation:**

Please refer to pages 1 and 2 of this report for a detailed discussion on the valuation method used in determining the Price Target.

February 22, 2005

**PUGET ENERGY, INC.**

PSD – NYSE

**Rating:****NEUTRAL****Price:** (2/22/05) \$23.04**Price Targets:**

12-18 month: \$23 ↓

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

406.791.7230

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FY (Dec)	2004A*	2005E	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,568.8	\$2,566.7	0%	\$2,515.5	-2%
Previous		\$2,564.1		\$2,507.4	
Price/Revenue ratio	.9x	.9x		.9x	
<b>EPS Revised</b>	<b>\$0.55</b>	<b>\$1.42</b>	158%	<b>\$1.64</b>	16%
Previous		\$1.53		\$1.70	
Price/EPS ratio	41.8x	16.2x		14.0x	
<b>EBITDA (\$M)</b>	\$542.8	\$661.8	22%	\$710.1	7%
EV/EBITDA ratio	9.0x	7.4x		6.9x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05E	<b>\$0.62</b>	\$0.69	\$801.5	\$802.8	\$207.5
6/30/05E	<b>\$0.15</b>	\$0.17	\$547.1	\$547.6	\$135.5
9/30/05E	<b>\$0.05</b>	\$0.06	\$437.8	\$438.9	\$113.0
12/31/05E	<b>\$0.60</b>	NC	\$780.4	\$774.7	\$205.7

\*See detail of footnote on page 2.

**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (9/30/04)	61.2%
Cash per share (9/30/04)	\$0.25
Book value per share (9/30/04)	\$16.67
Dividend (yield)	\$1.00 (4.3%)
Return on Equity (T-T-M)	3%

**Trading Data**

Shares outstanding (M)	99.7
Market Capitalization (\$M)	\$2,297
52-week range	\$20.51 - \$24.81
Average daily volume (3 mos.) (K)	250
Float	100%
Index Membership	S&P 400 MidCap

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

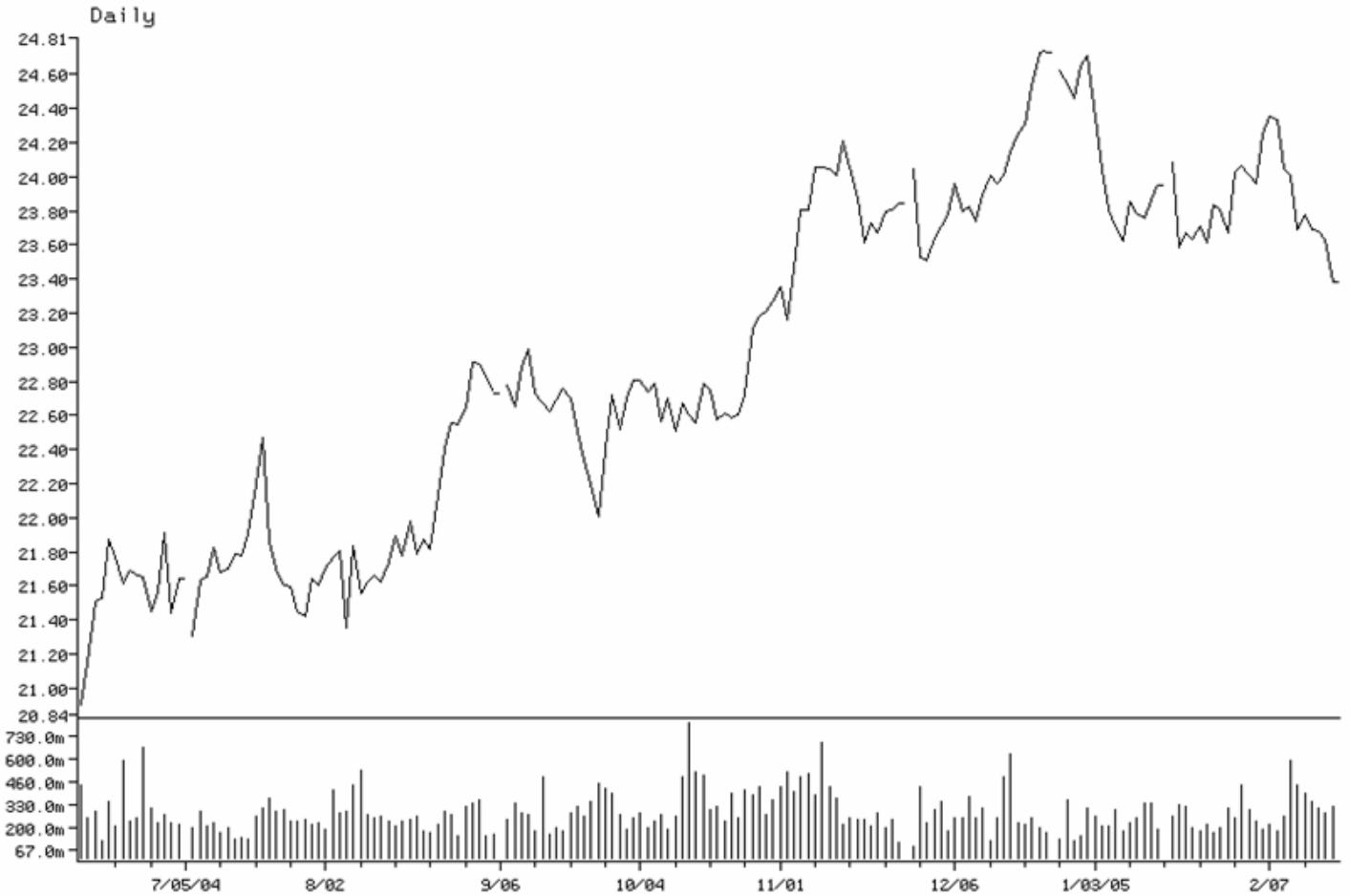
**Lowering EPS Estimates and Target in Wake of Rate Decision.**

- The Washington Utilities and Transportation Commission (WUTC) granted Puget Sound Energy an \$82.9 million increase in electric and gas rates, effective March 4, 2005. The utility had asked for rate relief of \$146.0 million (revised).
- The majority of the difference between what the company was granted and what it had requested is explained by the 10.3% return on equity allowed by the WUTC, compared to an 11.75% request, and an allowed equity ratio of 43% versus the 45% request. The utility's new rate base is \$3.6 billion.
- We are lowering our 2005 EPS estimate from \$1.53 to \$1.42 to better align our earnings model to the reality of the implied earnings power of the utility, derived by combining the new allowed rate base and ratios with the costs highlighted in the next bullet. Our estimate assumes InfrastruX contributes 1H'05 EPS of \$0.04 before being divested at mid-year.
- The company faces a 2005 regulatory lag of recovering rising costs not reflected in the rate order (-\$0.15 per share) and on-going disallowances of certain Tenaska gas costs (-\$0.07 per share). Also, earnings may be reduced by above-average temperatures experienced so far in 1Q'05. Factoring in the implications of the rate order, our 2006 EPS estimate is being lowered from \$1.70 to \$1.64.
- We are reducing our 12-18 month target price by a point to \$23, or 15.0x the average of our revised 2005 and 2006 EPS estimates. With the share price near this target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.3%.

Please refer to pages 5-6 of this report for detailed disclosure and certification information.



**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*Includes a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

	2000	2001	2002	2003	9/30/2004
<b>Assets</b>					
<b>Utility Plant:</b>					
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,361,504
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,845,141
Common plant	351,051	362,670	378,844	390,622	406,395
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,424,162)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,188,878
<b>Other Property and Investments:</b>					
Investment in Bonneville Exchange Power Contract	58,189	54,663	51,136	47,609	44,964
Goodwill, net	45,655	102,151	125,555	133,302	133,069
Intangibles, net		16,059	18,652	18,707	17,239
Non-utility property and equipment, net		48,369	80,855	91,932	95,024
Other	188,453	96,007	101,932	110,543	108,703
Total other property and investments	292,297	317,249	378,130	402,093	398,999
<b>Current Assets:</b>					
Cash	36,383	92,356	176,669	27,481	21,211
Restricted cash			18,871	2,537	3,777
Accounts receivable, net					
Less: Allowance for doubtful accounts					
Total accounts receivable	343,108	279,321	279,623	227,115	202,423
Unbilled revenues	211,784	147,008	112,115	131,798	75,928
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	117,081
Purchased gas receivable	96,050	37,228			18,172
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	33,386
Taxes receivable					
Prepayments and other	11,607	11,277	11,323	12,200	23,360
Total current assets	797,933	660,838	672,744	493,852	495,338
<b>Long-Term Assets:</b>					
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	135,662
PURPA buyout costs	243,071	244,635	243,584	227,753	215,369
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	25,076
Power cost adjustment mechanism				3,605	
Other	177,609	239,941	269,876	315,739	386,090
Total Long-term assets	628,030	680,909	690,388	698,513	762,197
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,845,412</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>					
Common stock	\$859,038	\$870	\$936	\$991	\$997
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,617,164
Earnings reinvested in the business	92,673	32,229	36,396	58,217	54,462
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(11,348)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,661,275
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,218,042
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,161,456
Minority interest in equity of a consolidated subsidiary			10,629	11,689	12,121
<b>Current Liabilities:</b>					
Accounts payable	410,619	167,426	205,619	214,357	165,052
Short-term debt	378,316	348,577	47,295	13,893	24,511
Current maturities of long-term debt	19,000	119,523	73,206	246,829	90,305
Purchased gas liability	0	0	83,811	11,984	
Accrued expenses:					
Taxes	103,996	70,708	62,562	77,451	26,568
Salaries and wages	17,445	14,746	11,441	12,712	12,594
Interest	43,955	42,505	37,942	32,954	41,018
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	4,270
Tenaska disallowance reserve					11,212
Other	26,685	46,178	47,761	46,378	46,498
Total current liabilities	1,000,016	844,808	572,047	660,194	422,028
Deferred Income Taxes	608,185	605,315	730,675	755,235	808,991
Other Deferred Credits	132,869	196,339	267,458	340,893	440,816
Commitments and Contingencies	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	0
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,845,412</b>

## PUGET SOUND ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)

	2003	1Q04	2Q04	3Q04	4Q04**	2004**	1Q05E	2Q05E	3Q05E	4Q05E	2005E	2006E
OPERATING REVENUES:												
Electric	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$1,423,033	\$406,573	\$319,230	\$338,896	\$442,955	\$1,507,655	\$1,587,317
Gas	634,230	275,692	119,479	89,432	284,703	769,306	314,075	131,593	97,397	335,908	878,973	922,137
Other	<u>347,830</u>	<u>75,283</u>	<u>93,369</u>	<u>102,850</u>	<u>104,971</u>	<u>376,473</u>	<u>80,850</u>	<u>96,250</u>	<u>1,500</u>	<u>1,500</u>	<u>180,100</u>	<u>6,000</u>
Total operating revenues	<u>2,382,803</u>	<u>743,470</u>	<u>515,939</u>	<u>514,951</u>	<u>794,452</u>	<u>2,568,812</u>	<u>801,499</u>	<u>547,073</u>	<u>437,793</u>	<u>780,363</u>	<u>2,566,728</u>	<u>2,515,454</u>
OPERATING EXPENSES:												
Energy costs:												
Purchased electricity	714,469	196,367	173,847	147,589	205,764	723,567	213,451	146,846	160,976	238,310	759,582	764,293
Purchased gas	327,132	162,407	63,703	44,574	180,618	451,302	194,839	72,540	51,263	214,885	533,527	571,659
Electric generation fuel	64,999	13,988	21,014	25,130	20,640	80,772	16,263	19,154	25,417	24,363	85,196	79,366
Residential Exchange	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(54,074)	(35,435)	(33,890)	(50,940)	(174,338)	(175,000)
Unrealized (gain)/loss on derivative instruments	106	(87)	(2,849)	1,894	516	(526)	0	0	0	0	0	0
Utility operations and maintenance	289,702	73,855	73,201	67,093	77,083	291,232	75,000	76,000	69,000	79,000	299,000	306,000
Other operations and maintenance	303,972	67,002	78,545	87,361	89,609	322,517	72,000	81,000	500	500	154,000	2,000
Depreciation and amortization	236,866	60,288	61,122	62,204	63,228	246,842	65,000	66,000	62,500	63,000	256,500	258,000
Merger and related costs/conservation amort.	33,458	8,190	4,809	4,747	4,942	22,688	8,000	5,000	5,000	5,000	23,000	24,000
Goodwill Impairment					91,196	91,196						
Taxes other than federal income taxes	208,395	67,492	45,622	46,024	62,843	221,981	69,000	47,000	47,000	64,000	227,000	235,000
Federal income taxes	<u>72,369</u>	<u>38,711</u>	<u>(2,929)</u>	<u>8,524</u>	<u>30,656</u>	<u>74,962</u>	<u>36,753</u>	<u>9,016</u>	<u>2,880</u>	<u>36,607</u>	<u>85,256</u>	<u>100,378</u>
Total operating expenses	2,077,628	633,790	480,723	461,126	776,421	2,352,060	696,232	487,121	390,646	674,724	2,248,723	2,165,696
OPERATING INCOME	305,175	109,680	35,216	53,825	18,031	216,752	105,267	59,952	47,147	105,639	318,005	349,758
OTHER INCOME	<u>1,564</u>	<u>64</u>	<u>1,586</u>	<u>318</u>	<u>2,324</u>	<u>4,292</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>2,000</u>	<u>2,000</u>
INCOME BEFORE INTEREST CHARGES	306,739	109,744	36,802	54,143	20,355	221,044	105,767	60,452	47,647	106,139	320,005	351,758
INTEREST CHARGES, net of AFUDC	183,973	43,399	43,270	42,834	43,496	172,999	43,750	45,000	42,750	45,250	176,750	184,000
Mandatorily redeemable securities interest	1,072	23	23	23	23	92	23	23	23	23	92	92
Minority interest	<u>177</u>	<u>(43)</u>	<u>289</u>	<u>162</u>	<u>(7,477)</u>	<u>(7,069)</u>	<u>150</u>	<u>150</u>	<u>0</u>	<u>0</u>	<u>300</u>	<u>600</u>
Discontinued Operations:												
NET INCOME before effect of acct. change	121,517	66,365	(6,780)	11,124	(15,687)	55,022	61,844	15,279	4,874	60,866	142,863	167,066
FAS-133 transition adjustment loss (net of tax)	169					0						
Less: Preferred stock dividends/ redemptions	<u>5,151</u>					<u>0</u>						
INCOME FOR COMMON STOCK	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$61,844	\$15,279	\$4,874	\$60,866	\$142,863	\$167,066
DILUTED COMMON SHARES OUT. --WEIGHTED	95,309	99,367	99,371	100,043	99,765	99,911	100,065	100,365	100,665	100,965	100,515	101,715
INCOME FOR COMMON STOCK												
Utility before accounting change	\$113,824	\$66,854	(\$9,634)	\$8,126	\$58,056	\$123,401	\$61,344	\$11,879	\$4,374	\$60,366	\$137,963	\$165,066
Cumulative effect of accounting change	169											
Non-utility	<u>2,204</u>	<u>(489)</u>	<u>2,854</u>	<u>2,998</u>	<u>(73,743)</u>	<u>(68,379)</u>	<u>500</u>	<u>3,400</u>	<u>500</u>	<u>500</u>	<u>4,900</u>	<u>2,000</u>
Total	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$61,844	\$15,279	\$4,874	\$60,866	\$142,863	\$167,066
EARNINGS PER COMMON SHARE												
Utility	\$1.19	\$0.67	(\$0.10)	\$0.08	\$0.58	\$1.24	\$0.61	\$0.12	\$0.04	\$0.60	\$1.37	\$1.62
Cumulative effect of accounting change	\$0.00											
Non-utility	<u>0.02</u>	<u>(0.00)</u>	<u>0.03</u>	<u>0.03</u>	<u>(0.74)</u>	<u>(0.68)</u>	<u>0.00</u>	<u>0.03</u>	<u>0.00</u>	<u>0.00</u>	<u>0.05</u>	<u>0.02</u>
DILUTED EARNINGS PER SHARE	\$1.22	\$0.67	(\$0.07)	\$0.11	(\$0.16)	\$0.55	\$0.62	\$0.15	\$0.05	\$0.60	\$1.42	\$1.64

\* Company adopted EITF 03-11 on Jan. 1, 2004, which requires most non-trading derivative instruments to be shown net in the income statement. For example, 1Q'03 "sales to other utilities & marketers," a subset of electric revenues, were shown originally as \$57.2 mm, and now are shown as \$21.9 mm. A similar offsetting adjustment was also made to lower purchased electric expenses, leaving net income unchanged. The company has now provided the quarterly reclassifications for 2003. \*\*Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

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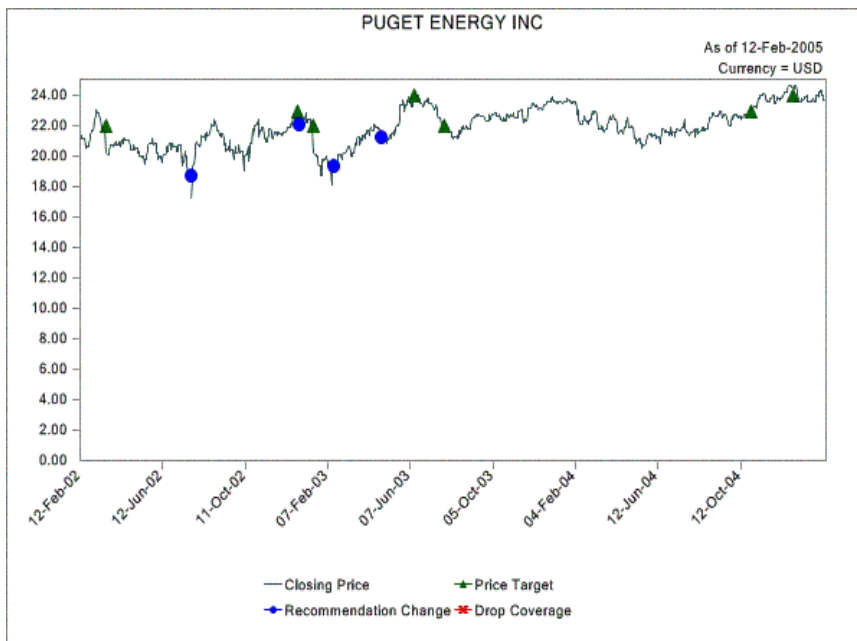
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D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 12/31/04)	Buy	Hold	Sell
Corresponding Institutional Research Rating	Buy	Neutral	Underperform
Distribution of Institutional Research Ratings	42%	45%	13%
Corresponding Retail Research Rating	Buy, Core/Buy	Hold, Core/Hold	Avoid
Distribution of Retail Research Ratings	71%	29%	0%
Distribution of combined ratings	47%	42%	11%
Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos	9%	8%	5%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
 Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
 Strong Buy, Buy, Neutral, Underperform

PUGET ENERGY INC					
Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	27-Dec-2004	24.62	24.00
14-Feb-2003	19.44	BUY	25-Oct-2004	22.71	23.00
26-Dec-2002	22.10	NEUTRAL	24-Jul-2003	22.05	22.00
22-Jul-2002	18.73	BUY	12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00
			21-Mar-2002	20.29	22.00

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

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**US Equity Research**  
J.P. Morgan Securities Inc.  
February 22, 2005

# Puget Energy

Rate Case Sets Stage To Build the Utility, Cutting Est.

## *Puget Energy*

**Overweight**

<i>Ticker</i>	<i>PSD</i>	<i>EPS</i>	<b>2004A</b>	<b>2005E (Old)</b>	<b>2005E (New)</b>	<b>2006E (Old)</b>	<b>2006E (New)</b>
<b>Price(02/18/05)</b>	\$23.38	<b>1Q (Mar)</b>	\$0.67				
<b>52-Wk.Range</b>	\$20.52-24.81	<b>2Q (Jun)</b>	\$0.16				
<b>Mkt.Cap(BN)</b>	\$2.33	<b>3Q (Sep)</b>	\$0.11				
<b>Fiscal Year</b>	Dec	<b>4Q (Dec)</b>	\$0.61				
<b>Shares O/S(MM)</b>	99.49	<b>FY</b>	\$1.60	\$1.65	\$1.50	\$1.80	\$1.70
<b>Div Yld</b>	4.28%	<b>P/E FY</b>	14.6	14.2	15.6	13.0	13.8

\*Official EPS estimates are rounded to the nearest \$0.05.

Puget was allowed a 10.3% ROE and a 43% equity layer on a \$3.6 Bn rate base on Friday. We now expect Puget to invest in and grow its electric rate base, offering investors attractive, relatively low-risk EPS growth. We are maintaining our Overweight rating

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- The Washinton Utility and Transportation Commission ruled in Puget's electric and gas rate case on Friday allowing the company a 10.3% ROE and a 43% equity layer on a \$3.6 billion rate base. We believe this now sets the stage for the company to invest in its utility infrastructure. We expect it to spend about \$1.3 billion (about 50% of electric rate base) over the next 7-10 years to build out its utility system.
- We expect Puget to be allowed to earn a return on its planned spending at the utility and believe this will result in an attractive EPS growth profile over the next several years. We expect Puget's next step in pursuit of this strategy will be filing of a Power Cost Only Rate Case to incorporate two wind farms it is pursuing into rate base. We assume the wind farms are added to rate base starting in 2006.
- We are lowering our 2005 EPS estimate to \$1.50 from \$1.65 and our 2006 EPS estimate to \$1.70 from \$1.80 to reflect the WUTC's rate case ruling. We would note that we believe the 13% year-over-year EPS growth we project (driven by a full year of rate relief as well as the addition of wind farms to rate base) illustrates the strong EPS growth Puget can drive by adding to its rate base.
- We believe Puget's EPS growth profile, is not reflected in the stock's valuation. Based on our DCF analysis, we believe Puget's shares are undervalued, and on a relative P/E basis, Puget looks undervalued as well. It is currently trading at about 14x our 2006 EPS estimate. This represents a discount to the industry average P/E multiple for 2006E of about 14.6x.

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- We also note that Puget offers a slightly above-average dividend return, so investors are paid to wait while its EPS growth materializes.

### **Valuation and Rating Analysis**

We believe Puget's EPS growth profile, as well as our forecast for 10% long-term EPS growth, is not reflected in the stock's current valuation. Based on our DCF analysis, we believe Puget's shares are undervalued, and on a relative P/E basis, Puget looks undervalued as well. It is currently trading at about 14x our 2006 EPS estimate. This represents a discount to the industry average P/E multiples for 2006E of about 14.6x. Furthermore, we note that Puget pays a dividend slightly above the industry average, so investors are paid to wait while Puget's EPS growth materializes.

### **Risks to Our Rating**

Our investment thesis for Puget's shares is based primarily on it being allowed to increase its rates to recover investment in its utility infrastructure, improve its utility ROE, and continue to improve its balance sheet. If Puget is not allowed to increase its rates to reflect investment in its utility, it will earn a utility ROE that is well below the industry average and will likely have difficulty further improving its balance sheet materially. In this case, our outlook for the shares would be less favorable.

### **Companies Recommended in This Report**

Puget Energy (PSD/\$23.38/Overweight)

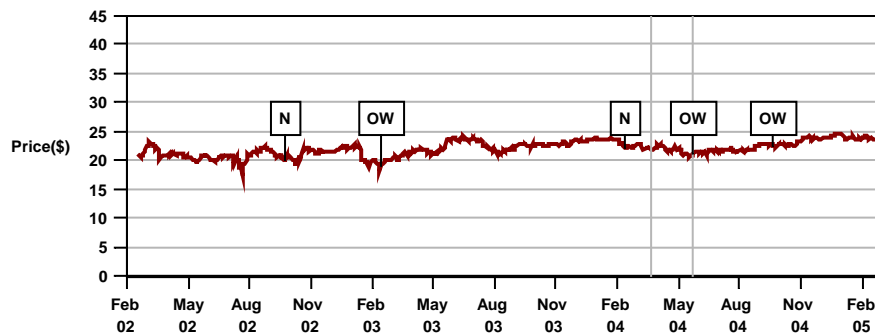
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Puget Energy (PSD) Price Chart



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.

Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.

JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

Ratings prior to Sept. 25, 2002: B = Buy, LTB = Long-Term Buy, MP = Market Performer, MU = Market Underperformer.

**Explanation of Ratings:** JPMorgan uses the following rating system: **Overweight** [Over the next six to twelve months, we expect this stock will outperform the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] **Neutral** [Over the next six to twelve months, we expect this stock will perform in line with the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] **Underweight** [Over the next six to twelve months, we expect this stock will underperform the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] The analyst or analyst's team's coverage universe is the sector and/or country shown on the cover of each publication. Each analyst's coverage list, showing full coverage universe, is available on the analyst's page under the Research option on JPMorgan's website [www.morganmarkets.com](http://www.morganmarkets.com), accessible to JPMorgan's clients via password, or in the case of hard copy research or if no access to MorganMarkets, by calling this toll free number (1-800-477-0406).

Prior to September 25, 2002, our rating system was: Buy — we expect the stock to outperform the market by a minimum of 5% within an investment horizon of one year; Long-Term Buy — we believe the stock will outperform the market over the long run, but we lack the visibility of a catalyst for outperformance within a one-year investment horizon; Market Performer — the stock is expected to perform in line with the market; Market Underperformer — we expect the stock to underperform the market by a minimum of 5% within an investment horizon of one year.

**JPMorgan Equity Research Ratings Distribution, as of December 31, 2004**

	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	39%	42%	19%
IB clients*	44%	44%	32%
JPMSI Equity Research Coverage	32%	49%	19%
IB clients*	64%	58%	43%

\*Percentage of investment banking clients in each rating category.

For purposes only of NASD/NYSE ratings distribution rules, our Overweight rating falls into a buy rating category; our Neutral rating falls into a hold rating category; and our Underweight rating falls into a sell rating category.

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Revised December 31, 2004.

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**▲ McAdams ▲ Wright ▲ Ragen ▲**  
 I N C O R P O R A T E D

02.22.2005

**RESEARCH**

Paul C. Latta, CFA > platta@mwrinc.com > 206.664.8897

**Puget Energy, Inc. (PSD) | \$23.38**

**Target Price: \$27.00 | BUY**

FUNDAMENTAL SNAPSHOT

52 Week High	\$24.81
52 Week Low	\$20.51
Shares Out (Mil)	99.7
Market Cap (Bil)	\$2.3

EARNINGS ESTIMATES

EPS	FY03A	FY04A	FY05E
FY	\$1.26	\$1.60	\$1.58

IMPLIED P/E RATIOS			
P/E	FY03A	FY04A	FY05E
FY	18.5x	14.6x	14.8x

**WUTC Approves Rate Increases**

- On Friday, the Washington Utilities and Transportation Committee (WUTC) approved rate increases for PSD's electric and gas utilities. Specifically the WUTC approved an electric and gas increase of \$56.6 million and \$26.3 million, respectively, and an allowed return of 10.3%.
- Not surprisingly, the final settlement ended up somewhere between the Company's original proposal and the WUTC Staff's first counterproposal. Specifically, the increase compares to PSD's original request of electric and gas increases \$81.6 million and \$34.3 million and an allowed return of 11.75%. And it compares to the WUTC Staff counterproposal of \$21.3 million and \$8.1 million and an allowed return of 9.0%.
- We believe the conclusion of the general rate case removes an element of regulatory risk from the stock. We continue to rate PSD Buy.

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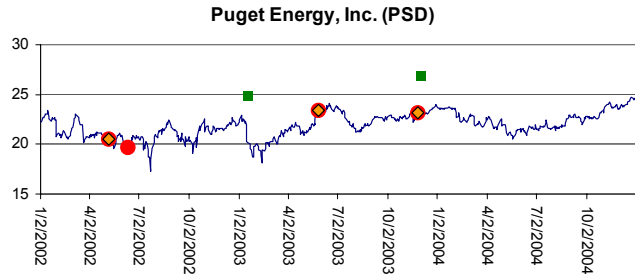
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	From	To	Date	Price
■	Price Target	\$25 to \$27	12/1/2003	\$23.48
◆	Added to Focus List		11/26/2003	\$23.21
●	Hold to	Buy	11/26/2003	\$23.21
◆	Removed from Focus List		5/28/2003	\$23.40
●	Buy to	Hold	5/28/2003	\$23.40
■	Price Target	To \$25	1/16/2003	\$20.24
●	Rating System Change	Buy	6/11/2002	\$19.64
◆	Added to Focus List		5/6/2002	\$20.57
●	Hold to	Buy	5/6/2002	\$20.57



● Ratings Change ◆ Focus List Change ■ Target Price Change

Price targets are subject to change as new information becomes available, and reflect our current judgment regarding this security. Note that there are risks that may impede the achievement of a predicted price target. Price targets are based on fundamental factors such as historical and projected earnings, cash flow, discounted cash flow, relative book value, peer group evaluation, relative sector valuations, and expectations on general market and economic conditions.

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 Hold/Addition to InStock Recommended List: We expect the Stock to be a Market Performer.  
 Sell/Removal from InStock Recommended List: We expect the Stock to Underperform the Market.  
 Ratings System in effect between 2/7/2002 and 6/12/2002: Strong Buy, Buy, Hold, Underperform, Sell.  
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	Percentage of Rated Stocks Currently Assigned this Rating	Percentage of Rated Stocks with this Rating with which MWR has had an Investment Banking Relationship in the last 12 months
Buy	51%	9%
Hold	36%	4%
Sell	13%	0%

For Price Chart and Ratings History disclosures, please go to <http://www.mwrinc.com/ClientAccess/quotesresearch.html>, or to request information, please contact Sara E. Hasan, Research Assistant, (206) 664-8854, [mwr@mwrinc.com](mailto:mwr@mwrinc.com)

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22 February 2005

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# Puget Energy Inc.

**Looks Like Break-Even****NEUTRAL****Reason for Report:** Final Order in General Rate Case**Volatility Risk:**  
**MEDIUM****Company****PSD; \$23.38; B-2-7**

EPS (Dec): 2004A \$1.60; 2005E \$1.60; 2006E NA  
P/E (Dec): 2004A 14.6x; 2005E 14.6x; 2006E NM

GAAP EPS (Dec): 2004A NA; 2005E NA; 2006E NA  
GAAP P/E (Dec): 2004A NM; 2005E NM; 2006E NM

**Event**

Late Friday, the Washington Utilities and Transportation Commission (WUTC) issued a final order in PSD's electric and gas general rate case, granting a revenue increase of \$56.6M for electric and \$26.2M for gas, based on a \$3.6B rate base earning 10.3% on a capital structure incorporating 43% equity. PSD requested hikes of \$81.6M electric and \$41.2M gas.

**Analysis**

Initial read...this is a decent order that, based on quick analysis of the foregoing numbers, should allow PSD to earn somewhere in the neighborhood of \$1.60 per share on a run-rate.

The new rates will become effective on March 4. Consistent with our expectations, this follows the winter season, meaning that the full impact of the rate increase won't be seen until next year. We're still evaluating the order, and so is the company.

Puget is currently under-earning its 11% allowed ROE, although the company has "maxed out" its power cost sharing mechanism's cumulative cap. We assume no earnings for InfrastruX, which PSD now plans to sell.

Based on the foregoing, we believe Puget should earn somewhere around \$1.55 to \$1.60 this year. The company is still evaluating the WUTC order, and isn't likely to offer 2005 guidance for another couple of weeks. However, it appears that our current \$1.68 estimate for this year is likely a bit on the high side. We are lowering our 2005 estimate to \$1.60, and will further refine that as warranted when PSD offers its current year outlook.

**Recommendation**

We remain Neutral. Shares are trading at 14.5X our current full-year estimated earning potential, or just under 14X if some growth and some construction period AFUDC on planned wind-based generation is factored in. The yield (dividend is unlikely to grow near-term) is just over 4%. On that basis, the stock appears fairly valued.

Changes at the WUTC are potentially significant. Governor Christine Gregoire appointed two new commissioners, replacing in the process incumbent Chair Marilyn Showalter. The significant capital investment needs faced by the state's two major investor-owned utilities will entail further rate filings, as additional financing. The state's regulatory tenor will have a significant bearing on share performance, and ultimately on utility financing costs.

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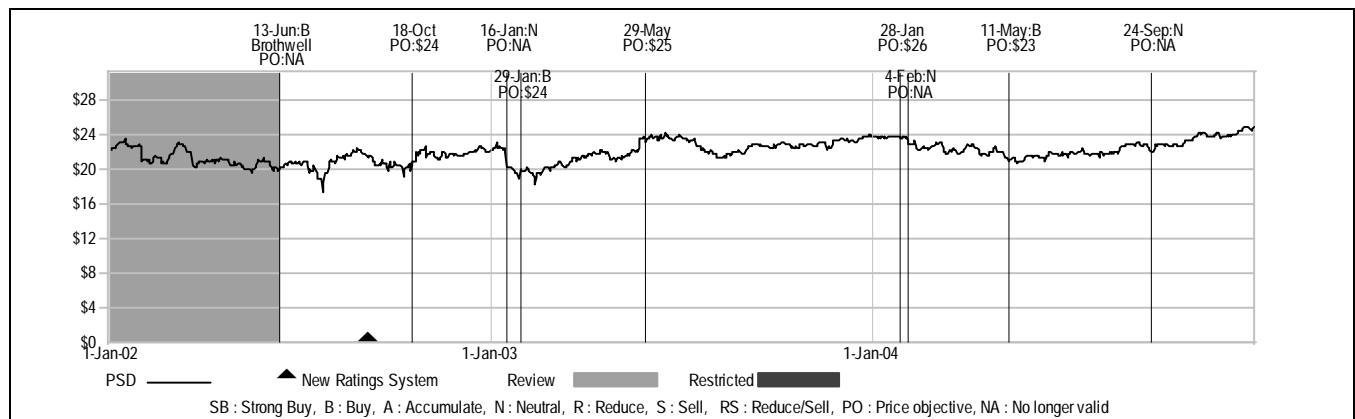
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PSD Price Chart



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Investment Rating Distribution: Energy Group (as of 31 December 2004)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	47.06%	Buy	28	38.89%
Neutral	76	49.67%	Neutral	29	38.16%
Sell	5	3.27%	Sell	0	0.00%
Investment Rating Distribution: Global Group (as of 31 December 2004)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1054	40.45%	Buy	383	36.34%
Neutral	1339	51.38%	Neutral	382	28.53%
Sell	213	8.17%	Sell	43	20.19%

\* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

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# UBS Investment Research

## Puget Energy Inc.

 Electric Utilities  
**Rating** **Neutral 2**  
*Unchanged*
**Price target** **US\$23.00**  
*Prior: US\$24.00*
**Price** **US\$22.88**

RIC: PSD.N BBG: PSD US

**23 February 2005**
**Trading data**

52-wk. range	US\$24.73-20.54
Market cap.	US\$2.28bn
Shares o/s	99.7m
Free float	80%
Avg. daily volume ('000)	215
Avg. daily value (US\$m)	5.1

**Balance sheet data 12/05E**

Shareholders' equity	US\$1.77bn
P/BV (UBS)	1.3x
Net cash (debt)	(US\$2.61bn)

**Forecast returns**

Forecast price appreciation	+0.5%
Forecast dividend yield	4.4%
Forecast stock return	+4.9%
Market return assumption	8.4%
Forecast excess return	-3.5%

**EPS (UBS, US\$)**

	12/05E		Cons.	12/04 Actual
	From	To		
Q1E	0.71	0.68	0.65	0.67
Q2E	0.17	0.16	0.15	0.16
Q3E	0.09	0.09	0.08	0.11
Q4E	0.60	0.58	0.61	0.61
12/05E	1.55	1.50	1.57	
12/06E	1.70	1.70	1.65	

### Rate Order Released

#### PSD Receives Electric and Gas Rate Case Decision

Last Friday, the Washington Utilities and Transportation Commission (WUTC) authorized PSD to increase electric and gas rates by \$56.6 million and \$26.3 million, respectively. This was based on a 10.3% ROE and a 43% equity ratio versus PSD's request of 11.75% ROE and 45% equity ratio.

#### Authorized ROE Lower Than Our Expectation

The overall rate increase was roughly in-line with our est.; however, an authorized ROE below the previous level of 11% was disappointing. While this does not impact our '05 est. significantly, it does change our view with respect to the return PSD could earn on future rate base additions. Under its Least Cost Plan (LCP), PSD is expected to add over 1000 MW of generation over the next decade.

#### Lowering 2005 EPS Estimate

We are lowering our recurring 2005E EPS to \$1.50 from \$1.55, to reflect a modest \$0.03 impact of the rate order and \$0.02 for a warmer than normal start to the year. We are maintaining our 2006 est. at \$1.70.

#### Valuation: Lowering 12-month Price Target to \$23 from \$24

Our new reduced ROE assumption lowers the net present value of the LCP in our overall DCF analysis. Our new \$23 PT implies a 13.5x PE on 2006E EPS or a modest discount to peers, which we deem appropriate since high leverage and LCP execution risks offset above average EPS growth from the addition of new generation.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,601	2,795	-
EBIT	377	418	428	455	-
Net income (UBS)	110	155	152	171	-
EPS (UBS, US\$)	1.16	1.55	1.50	1.70	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	16.5	16.3	-
ROIC (EBIT) %	-	9.3	9.3	9.9	-
EV/EBITDA x	-	6.9	6.6	6.4	-
PE (UBS) x	-	14.6	15.3	13.5	-
Dividend yield %	-	4.4	4.4	4.4	-

Source: UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$22.88 on 22 Feb 2005

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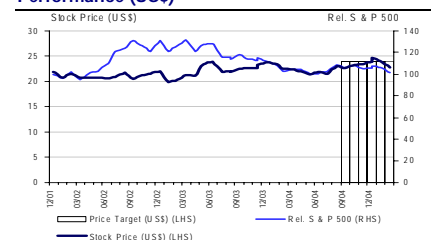
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**Performance (US\$)**


Source: UBS

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■ **Puget Energy Inc.**

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. InfrastruX provides infrastructure construction services to the electric and gas utility industries.

■ **Statement of Risk**

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.

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<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	53%	35%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	29%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 31 December 2004.

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**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

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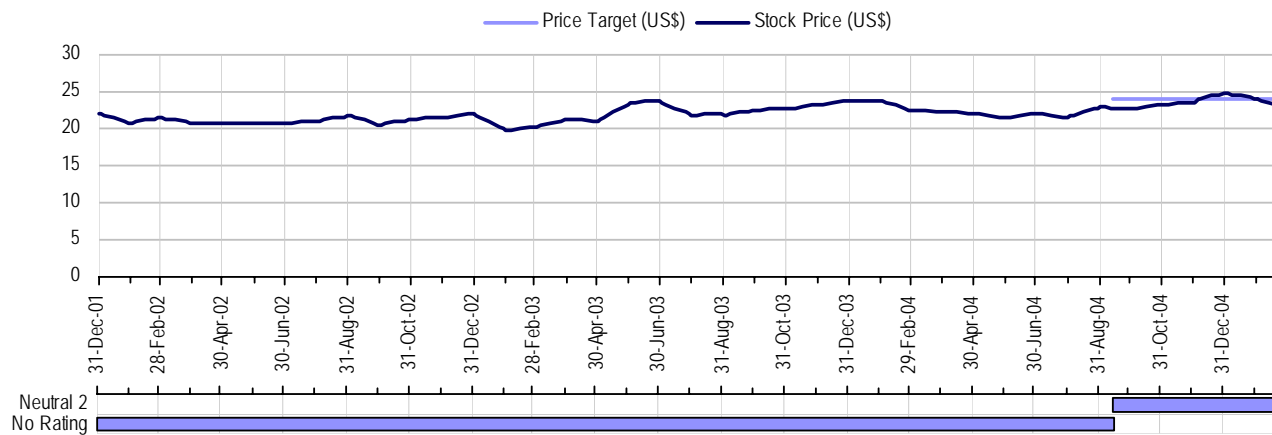
### Companies mentioned

Company Name	Reuters	Rating	Price
Puget Energy Inc. <sup>4,5,6a,6b,6c,7,16</sup>	PSD.N	Neutral 2	US\$22.88

Price(s) as of 22 February 2005. Source: UBS.

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**Puget Energy Inc. (US\$)**



Source: UBS; as of 22 February 2005.

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**US Equity Research**

J.P. Morgan Securities Inc.  
March 10, 2005

# Puget Energy

## Issues 2005-2006 Guidance

### *Puget Energy*

**Overweight**

<i>Ticker</i>	<i>PSD</i>	<i>EPS</i>	<b>2004A</b>	<b>2005E</b>	<b>2006E</b>
<b>Price(03/10/05)</b>	\$23.30	<b>1Q (Mar)</b>	\$0.67		
<b>52-Wk.Range</b>	\$20.52-24.81	<b>2Q (Jun)</b>	\$0.16		
<b>Mkt.Cap(BN)</b>	\$2.32	<b>3Q (Sep)</b>	\$0.11		
<b>Fiscal Year</b>	Dec	<b>4Q (Dec)</b>	\$0.61		
<b>Shares O/S(MM)</b>	99.49	<b>FY</b>	\$1.60	\$1.50	\$1.70
<b>Div Yld</b>	4.29%	<b>P/E FY</b>	14.6	15.5	13.7

\*Official EPS estimates are rounded to the nearest \$0.05.

PSD introduced 2005 and 2006 EPS guidance after the close today. After reviewing comments management made at a conference today, we believe this guidance should be adjusted for non-recurring items as well as the recovery of rate base investment.

- PSD initiated 2005 EPS guidance of \$1.30-1.40. The company is holding a conference call tomorrow (3/11) to discuss further details, but at first glance we believe a couple of items should be considered. First, we believe \$0.07 related to the Tenaska disallowance is non-recurring, and secondly, it appears management has assumed some dilution for an equity issuance to fund wind generation construction.
- We also believe there are items to be considered when looking at PSD's 2006 EPS guidance of \$1.40-1.55. Again, we believe \$0.05 per share related to the Tenaska disallowance should be considered non-recurring. We also note that management has not included about \$0.13 per share expected to come from a \$310M addition to rate base for new wind generation.
- PSD hosts a call tomorrow (3/11) at 10:00a.m., and we are looking for further details regarding the drivers for 2005 and 2006 EPS guidance. At first glance and based on comments by the company at a conference this afternoon, we believe there are reasonable adjustments to be made that bring our current estimates more inline with this guidance. The call in details are 888-396-2356; ID: Puget.
- If 2005 and 2006 EPS guidance is adjusted for the items discussed above, and we assume an equity offering in in 2005 to fund 43% of the construction of wind generation (we'd previously assumed an issuance in early 2006), management guidance is similar to our estimates.

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### **Valuation and Rating Analysis**

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We believe Puget's EPS growth profile, as well as our forecast for 10% long-term EPS growth, is not reflected in the stock's current valuation. Based on our DCF analysis, we believe Puget's shares are undervalued, and on a relative P/E basis, Puget looks undervalued as well. It is currently trading at about 14x our 2006 EPS estimate. This represents a discount to the industry average P/E multiples for 2006E of about 14.5x. Furthermore, we note that Puget pays a dividend slightly above the industry average, so investors are paid to wait while Puget's EPS growth materializes.

### Risks to Our Rating

Our investment thesis for Puget's shares is based primarily on it being allowed to increase its rates to recover investment in its utility infrastructure, improve its utility ROE, and continue to improve its balance sheet. If Puget is not allowed to increase its rates to reflect investment in its utility, it will earn a utility ROE that is well below the industry average and will likely have difficulty further improving its balance sheet materially. In this case, our outlook for the shares would be less favorable.

### Companies Recommended in This Report

Puget Energy (PSD/\$23.30/Overweight)

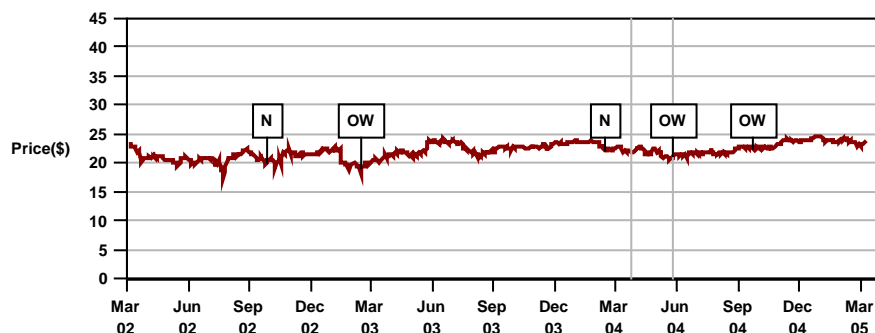
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Puget Energy (PSD) Price Chart



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.

Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.

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Prior to September 25, 2002, our rating system was: Buy — we expect the stock to outperform the market by a minimum of 5% within an investment horizon of one year; Long-Term Buy — we believe the stock will outperform the market over the long run, but we lack the visibility of a catalyst for outperformance within a one-year investment horizon; Market Performer — the stock is expected to perform in line with the market; Market Underperformer — we expect the stock to underperform the market by a minimum of 5% within an investment horizon of one year.

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	<b>Overweight (buy)</b>	<b>Neutral (hold)</b>	<b>Underweight (sell)</b>
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IB clients*	44%	44%	32%
JPMSI Equity Research Coverage	32%	49%	19%
IB clients*	64%	58%	43%

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**PUGET ENERGY, INC.**

PSD – NYSE

March 11, 2005

**Rating:****NEUTRAL****Price:** (3/11/05) \$22.78**Price Targets:**

12-18 month: \$23

5-year: \$30

**Industry:**

Utilities

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FY (Dec)	2004A*	2005E*	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,568.8	\$2,566.7	0%	\$2,515.5	-2%
Previous		NC		NC	
Price/Revenue ratio	.9x	.9x		1.0x	
<b>EPS Revised</b>	<b>\$0.55</b>	<b>\$1.42</b>	158%	<b>\$1.50</b>	6%
Previous		NC		\$1.64	
Price/EPS ratio	41.4x	16.0x		15.2x	
<b>EBITDA (\$M)</b>	\$542.8	\$661.8	22%	\$700.5	6%
EV/EBITDA ratio	8.8x	7.2x		6.8x	

<u>Quarterly Data:</u>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05E	<b>\$0.62</b>	NC	\$801.5	NC	\$207.5
6/30/05E	<b>\$0.15</b>	NC	\$547.1	NC	\$135.5
9/30/05E	<b>\$0.05</b>	NC	\$437.8	NC	\$113.0
12/31/05E	<b>\$0.60</b>	NC	\$780.4	NC	\$205.7

\*See detail of footnote on page 2.

**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (12/31/04)	61.0%
Cash per share (12/30/04)	\$0.21
Book value per share (12/31/04)	\$16.24
Dividend (yield)	\$1.00 (4.4%)
Return on Equity (T-T-M)	3%

**Trading Data**

Shares outstanding (M)	99.9
Market Capitalization (\$M)	\$2,275
52-week range	\$20.51 - \$24.81
Average daily volume (3 mos.) (K)	245
Float	100%
Index Membership	S&P 400 MidCap

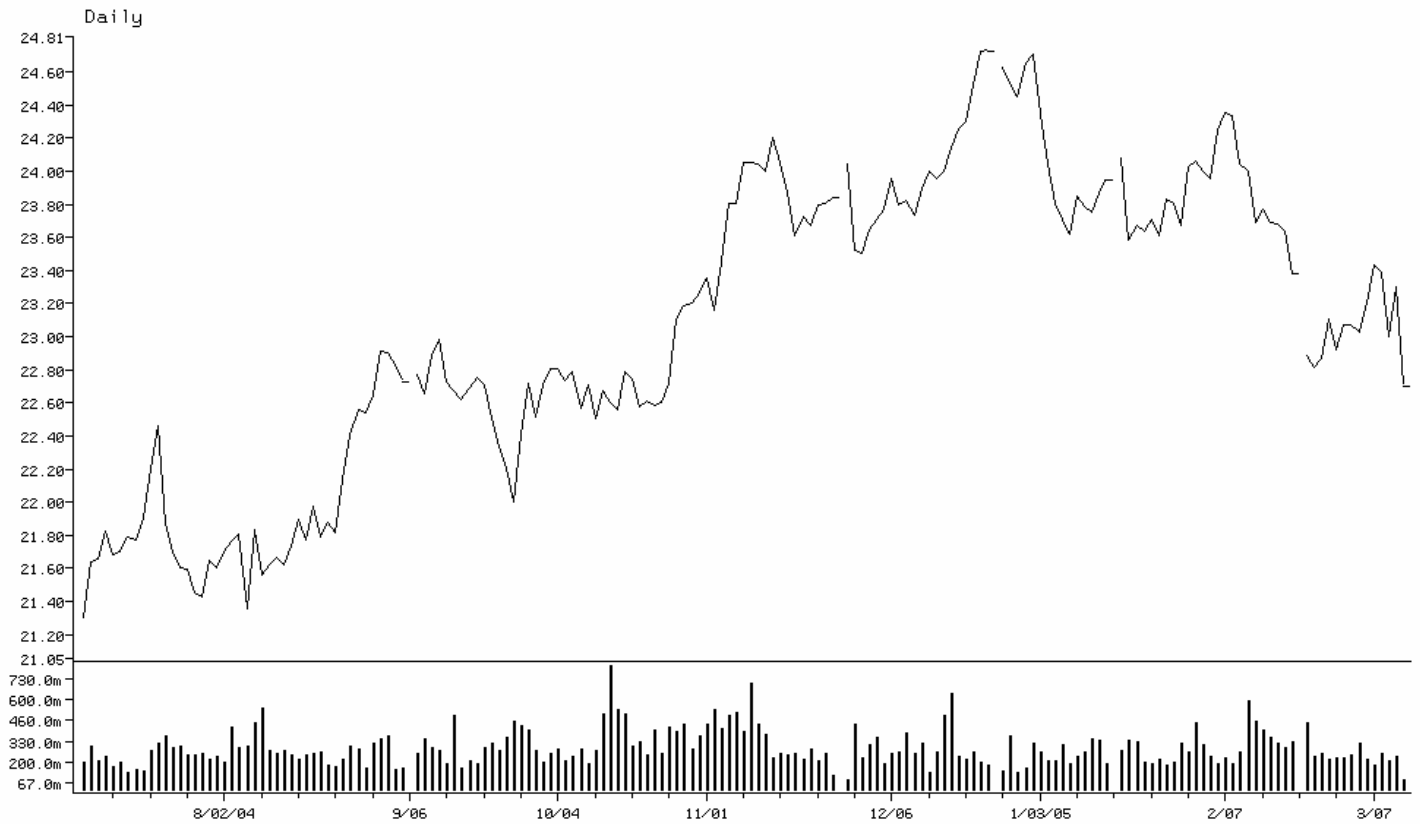
**Reducing EPS Forecast for Potential Share Offering and Regulatory Lag. Maintaining Target Price and NEUTRAL Rating.**

- With the recent conclusion of a general rate case, Puget Energy is introducing EPS guidance from continuing operations of \$1.30-\$1.40 and \$1.40-\$1.55 for 2005 and 2006, respectively.
- We are maintaining our 2005 EPS of \$1.42. (See our *Research Bulletin* of February 22, 2005.) This estimate assumes a contribution of \$0.04 per share from InfrastruX before that business is divested later in 2005. InfrastruX is being classified in discontinued operations and is not included in the EPS guidance. However, our earnings model continues to show InfrastruX in operations since the historical restatement for this reclassification has not yet been provided.
- We are lowering our 2006 EPS estimate from \$1.64 to \$1.50. Half of the EPS reduction is attributed to an assumption that the company has a year-end 2005 share offering of approximately five million shares to move its equity ratio to approximately 43% and to help fund two wind power projects. The other half of the reduction is associated with more earnings drag from regulatory lag and the Tenaska gas cost disallowance than our previous forecast.
- We are maintaining our 12-18 month target price of \$23, or 15.3x our revised 2006 EPS estimates. With the share price near this target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.4%.

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*2004 results include a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

\*\*2005 results include an EPS contribution of \$0.04/sh. from InfrastruX, which is being classified in discontinued operations.

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

**Assets**

	2000	2001	2002	2003	2004
<b>Utility Plant:</b>					
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,389,882
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,881,768
Common plant	351,051	362,670	378,844	390,622	409,677
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,452,969)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,228,358
<b>Other Property and Investments:</b>					
Investment in Bonneville Exchange Power Contract	58,189	54,663	51,136	47,609	
Goodwill, net	45,655	102,151	125,555	133,302	43,503
Intangibles, net		16,059	18,652	18,707	16,680
Non-utility property and equipment, net		48,369	80,855	91,932	
Other	188,453	96,007	101,932	110,543	257,785
Total other property and investments	292,297	317,249	378,130	402,093	317,968
<b>Current Assets:</b>					
Cash	36,383	92,356	176,669	27,481	19,771
Restricted cash			18,871	2,537	1,633
Accounts receivable, net					
Less: Allowance for doubtful accounts					
Total accounts receivable	343,108	279,321	279,623	227,115	216,304
Unbilled revenues	211,784	147,008	112,115	131,798	140,391
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	107,356
Purchased gas receivable	96,050	37,228			19,088
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	8,087
Taxes receivable					
Prepayments and other	11,607	11,277	11,323	12,200	20,360
Total current assets	797,933	660,838	672,744	493,852	532,990
<b>Long-Term Assets:</b>					
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	127,252
PURPA buyout costs	243,071	244,635	243,584	227,753	211,241
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	13,765
Power cost adjustment mechanism				3,605	
Other	177,609	239,941	269,876	315,739	401,795
Total Long-term assets	628,030	680,909	690,388	698,513	754,053
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,833,369</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>					
Common stock	\$859,038	\$870	\$936	\$991	\$999
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,621,756
Earnings reinvested in the business	92,673	32,229	36,396	58,217	13,853
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(14,332)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,622,276
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,212,532
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,116,947
Minority interest in equity of a consolidated subsidiary			10,629	11,689	4,648
<b>Current Liabilities:</b>					
Accounts payable	410,619	167,426	205,619	214,357	239,520
Short-term debt	378,316	348,577	47,295	13,893	8,297
Current maturities of long-term debt	19,000	119,523	73,206	246,829	38,933
Purchased gas liability	0	0	83,811	11,984	
Accrued expenses:					
Taxes	103,996	70,708	62,562	77,451	77,698
Salaries and wages	17,445	14,746	11,441	12,712	13,829
Interest	43,955	42,505	37,942	32,954	29,005
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	19,261
Tenaska disallowance reserve					3,156
Other	26,685	46,178	47,761	46,378	61,155
Total current liabilities	1,000,016	844,808	572,047	660,194	490,854
Deferred Income Taxes	608,185	605,315	730,675	755,235	810,726
Other Deferred Credits	132,869	196,339	267,458	340,893	409,945
Commitments and Contingencies	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	249
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,833,369</b>

## % of Capitalization

Total debt and mandatory redemption preferred	64.7%	67.4%	62.3%	60.3%	61.0%
Preferred stock	1.4%	1.4%	1.4%	0.0%	0.0%
Common stock	33.9%	31.2%	36.3%	39.7%	39.0%
	100.0%	100.0%	100.0%	100.0%	100.0%

Shares outstanding (000's)	85,904	87,023	93,643	99,074	99,868
Book value per share	\$16.61	\$15.66	\$16.27	\$16.71	\$16.24
Book value per share for the utility			\$15.23	\$15.70	\$15.95

## PUGET SOUND ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)	2003	1Q04	2Q04	3Q04	4Q04**	2004**	1Q05E	2Q05E	3Q05E	4Q05E	2005E	2006E
<b>OPERATING REVENUES:</b>												
Electric	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$1,423,033	\$406,573	\$319,230	\$338,896	\$442,955	\$1,507,655	\$1,587,317
Gas	634,230	275,692	119,479	89,432	284,703	769,306	314,075	131,593	97,397	335,908	878,973	922,137
Other	<u>347,830</u>	<u>75,283</u>	<u>93,369</u>	<u>102,850</u>	<u>104,971</u>	<u>376,473</u>	<u>80,850</u>	<u>96,250</u>	<u>1,500</u>	<u>1,500</u>	<u>180,100</u>	<u>6,000</u>
Total operating revenues	<u>2,382,803</u>	<u>743,470</u>	<u>515,939</u>	<u>514,951</u>	<u>794,452</u>	<u>2,568,812</u>	<u>801,499</u>	<u>547,073</u>	<u>437,793</u>	<u>780,363</u>	<u>2,566,728</u>	<u>2,515,454</u>
<b>OPERATING EXPENSES:</b>												
Energy costs:												
Purchased electricity	714,469	196,367	173,847	147,589	205,764	723,567	213,451	146,846	160,976	238,310	759,582	777,785
Purchased gas	327,132	162,407	63,703	44,574	180,618	451,302	194,839	72,540	51,263	214,885	533,527	557,827
Electric generation fuel	64,999	13,988	21,014	25,130	20,640	80,772	16,263	19,154	25,417	24,363	85,196	87,302
Residential Exchange	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(54,074)	(35,435)	(33,890)	(50,940)	(174,338)	(175,000)
Unrealized (gain)/loss on derivative instruments	106	(87)	(2,849)	1,894	516	(526)	0	0	0	0	0	0
Utility operations and maintenance	289,702	73,855	73,201	67,093	77,083	291,232	75,000	76,000	69,000	79,000	299,000	310,000
Other operations and maintenance	303,972	67,002	78,545	87,361	89,609	322,517	72,000	81,000	500	500	154,000	2,000
Depreciation and amortization	236,866	60,288	61,122	62,204	63,228	246,842	65,000	66,000	62,500	63,000	256,500	260,000
Merger and related costs/conservation amort.	33,458	8,190	4,809	4,747	4,942	22,688	8,000	5,000	5,000	5,000	23,000	24,000
Goodwill Impairment					91,196	91,196						
Taxes other than federal income taxes	208,395	67,492	45,622	46,024	62,843	221,981	69,000	47,000	47,000	64,000	227,000	233,000
Federal income taxes	<u>72,369</u>	<u>38,711</u>	<u>(2,929)</u>	<u>8,524</u>	<u>30,656</u>	<u>74,962</u>	<u>36,753</u>	<u>9,016</u>	<u>2,880</u>	<u>36,607</u>	<u>85,256</u>	<u>95,861</u>
Total operating expenses	2,077,628	633,790	480,723	461,126	776,421	2,352,060	696,232	487,121	390,646	674,724	2,248,723	2,172,775
<b>OPERATING INCOME</b>	305,175	109,680	35,216	53,825	18,031	216,752	105,267	59,952	47,147	105,639	318,005	342,678
<b>OTHER INCOME</b>	1,564	64	1,586	318	2,324	4,292	500	500	500	500	2,000	2,000
<b>INCOME BEFORE INTEREST CHARGES</b>	306,739	109,744	36,802	54,143	20,355	221,044	105,767	60,452	47,647	106,139	320,005	344,678
<b>INTEREST CHARGES, net of AFUDC</b>	183,973	43,399	43,270	42,834	43,496	172,999	43,750	45,000	42,750	45,250	176,750	184,000
Mandatorily redeemable securities interest	1,072	23	23	23	23	92	23	23	23	23	92	92
Minority interest	<u>177</u>	<u>(43)</u>	<u>289</u>	<u>162</u>	<u>(7,477)</u>	<u>(7,069)</u>	<u>0</u>	<u>290</u>	<u>0</u>	<u>0</u>	<u>290</u>	<u>0</u>
Discontinued Operations:												
NET INCOME before effect of acct. change	121,517	66,365	(6,780)	11,124	(15,687)	55,022	61,994	15,139	4,874	60,866	142,873	160,586
FAS-133 transition adjustment loss (net of tax)	169					0						
Less: Preferred stock dividends/ redemptions	<u>5,151</u>					<u>0</u>						
<b>INCOME FOR COMMON STOCK</b>	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$61,994	\$15,139	\$4,874	\$60,866	\$142,873	\$160,586
<b>DILUTED COMMON SHARES OUT. --WEIGHTED</b>	95,309	99,367	99,371	100,043	99,765	99,911	100,065	100,365	100,665	100,965	100,515	106,915
<b>INCOME FOR COMMON STOCK</b>												
Utility before accounting change	\$113,824	\$66,854	(\$9,634)	\$8,126	\$58,056	\$123,401	\$61,494	\$11,739	\$4,374	\$60,366	\$137,973	\$158,586
Cumulative effect of accounting change	169											
Non-utility	<u>2,204</u>	<u>(489)</u>	<u>2,854</u>	<u>2,998</u>	<u>(73,743)</u>	<u>(68,379)</u>	<u>500</u>	<u>3,400</u>	<u>500</u>	<u>500</u>	<u>4,900</u>	<u>2,000</u>
Total	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$61,994	\$15,139	\$4,874	\$60,866	\$142,873	\$160,586
<b>EARNINGS PER COMMON SHARE</b>												
Utility	\$1.19	\$0.67	(\$0.10)	\$0.08	\$0.58	\$1.24	\$0.61	\$0.12	\$0.04	\$0.60	\$1.37	\$1.48
Cumulative effect of accounting change	\$0.00											
Non-utility	<u>0.02</u>	<u>(0.00)</u>	<u>0.03</u>	<u>0.03</u>	<u>(0.74)</u>	<u>(0.68)</u>	<u>0.00</u>	<u>0.03</u>	<u>0.00</u>	<u>0.00</u>	<u>0.05</u>	<u>0.02</u>
<b>DILUTED EARNINGS PER SHARE</b>	\$1.22	\$0.67	(\$0.07)	\$0.11	(\$0.16)	\$0.55	\$0.62	\$0.15	\$0.05	\$0.60	\$1.42	\$1.50

\* Company adopted EITF 03-11 on Jan. 1, 2004, which requires most non-trading derivative instruments to be shown net in the income statement. For example, 1Q'03 "sales to other utilities & marketers," a subset of electric revenues, were shown originally as \$57.2 mm, and now are shown as \$21.9 mm. A similar offsetting adjustment was also made to lower purchased electric expenses, leaving net income unchanged. The company has now provided the quarterly reclassifications for 2003. \*\*Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

D.A. Davidson & Co.

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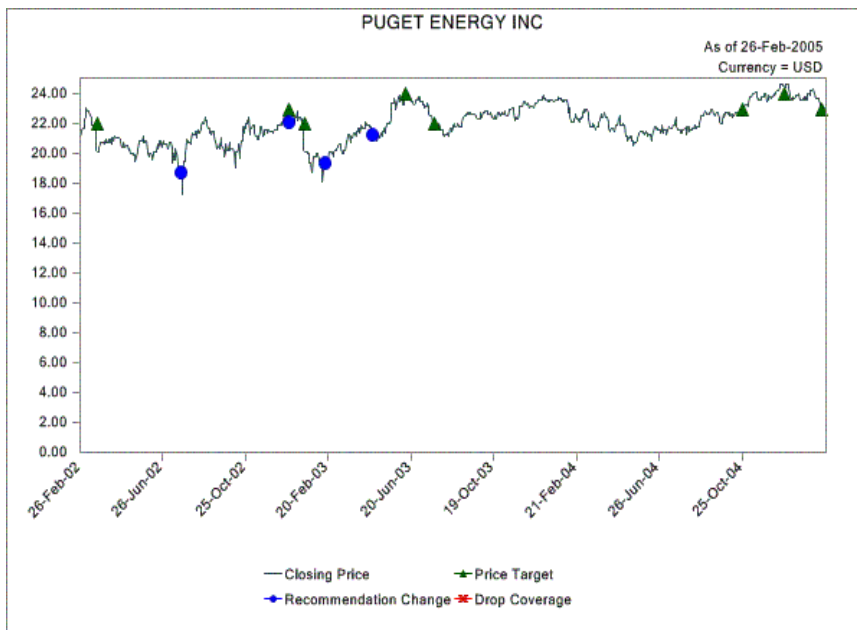
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I, James L. Bellessa, Jr., CFA, attest that (i) all the views expressed in this research report accurately reflect my personal views about the common stock of the subject company, and (ii) no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

### Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 12/31/04)	Buy	Hold	Sell
Corresponding Institutional Research Rating	Buy	Neutral	Underperform
Distribution of Institutional Research Ratings	42%	45%	13%
Corresponding Retail Research Rating	Buy, Core/Buy	Hold, Core/Hold	Avoid
Distribution of Retail Research Ratings	71%	29%	0%
Distribution of combined ratings	47%	42%	11%
Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos	9%	8%	5%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
Strong Buy, Buy, Neutral, Underperform

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
22-Jul-2002	18.73	BUY	24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00
			21-Mar-2002	20.29	22.00

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

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**▲ McAdams ▲ Wright ▲ Ragen ▲**  
 I N C O R P O R A T E D

03.11.2005

**RESEARCH**

Paul C. Latta, CFA > platta@mwrinc.com > 206.664.8897

**Puget Energy, Inc. (PSD) | \$22.72 Target Price: \$26.00 | BUY**

FUNDAMENTAL SNAPSHOT

52 Week High	\$24.81
52 Week Low	\$20.51
Shares Out (Mil)	99.7
Market Cap (Mil)	\$2,265.2

EARNINGS ESTIMATES

EPS	FY04A	FY05E	FY06E
FY	\$1.60	\$1.35	\$1.48

IMPLIED P/E RATIOS			
P/E	FY04A	FY05E	FY06E
FY	14.2x	16.8x	15.4x

**Management Provides 2005 Guidance**

- Puget Energy provided its first earnings guidance for 2005 of between \$1.30 and \$1.40 per share. The guidance was generally lower than most analysts' estimates. The street range was from \$1.36 to \$1.75 with a mean of \$1.56. Our estimate was \$1.58.
- The recent rate case called for a 10.3% return on equity and a 43% theoretical equity ratio on a \$3.6 billion rate base (\$2.5 billion for gas and \$1.1 billion for electric). Hence, based on the 99.7 million shares outstanding, theoretical base case earnings for the Company is now \$1.60 per share. Prior to the rate case settlement and Q4 earnings release, our base case earnings estimate for Puget Energy was \$1.80, which included \$0.12 in contribution from the now discontinued InfrastruX.
- Earnings in 2005 will be impacted by \$0.20 to \$0.30 due to costs associated with Tenaska, as well as depreciation and amortization (D&A) and operations and maintenance (O&M) costs. These costs are slightly higher than we noted in our previous report on PSD. Earnings for 2006 will be impacted by the same factors albeit to a lesser extent. Guidance for 2006 is for earnings per share of between \$1.40 and \$1.55 per share. Guidance for 2005 and 2006 does not include discontinued operations associated with InfrastruX, which is expected to be sold, or partnered by the end of this year. Management reiterated that the drought conditions in the Pacific Northwest will *not* impact 2005 results as the Company's power cost tracker allows higher purchased power costs to be passed through to ratepayers.
- We are lowering our 2005 estimate to \$1.35 from \$1.58 reflecting the new management guidance. Note that our estimate includes \$0.07 in costs from the above-mentioned Tenaska disallowance. (In 2004, First Call excluded Tenaska disallowances from the consensus estimates, although it is unclear whether First Call will exclude these costs in the 2005 consensus estimates.) We are rolling out a new 2006 estimate of \$1.48 per share. With the lower earnings, we are also shaving our price target to \$26 from \$27. While the earnings revision was a bit deeper than we feared going into the rate case, we would note that the regulatory risk is largely in the rear view mirror now and that there appears to be some upside revision potential to the earnings estimates. Hence, we continue to rate the stock Buy.

Paul C. Latta, CFA, platta@mwrinc.com, (206) 664-8897

- I, Paul C. Latta, hereby certify (1) that the views in this research note accurately reflect my personal views about any or all of the subject securities or issuers referred to in this note and (2) no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views in this note.

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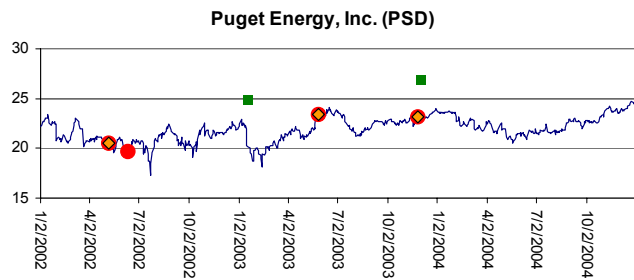
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**Required Disclosures:**

	From	To	Date	Price
■	Price Target	\$25 to \$27	12/1/2003	\$23.48
◆	Added to Focus List		11/26/2003	\$23.21
●	Hold to Buy	Buy	11/26/2003	\$23.21
◆	Removed from Focus List		5/28/2003	\$23.40
●	Buy to Hold	Hold	5/28/2003	\$23.40
■	Price Target	To \$25	1/16/2003	\$20.24
●	Rating System Change	Buy	6/11/2002	\$19.64
◆	Added to Focus List		5/6/2002	\$20.57
●	Hold to Buy	Buy	5/6/2002	\$20.57

● Ratings Change ◆ Focus List Change ■ Target Price Change



Price targets are subject to change as new information becomes available, and reflect our current judgment regarding this security. Note that there are risks that may impede the achievement of a predicted price target. Price targets are based on fundamental factors such as historical and projected earnings, cash flow, discounted cash flow, relative book value, peer group evaluation, relative sector valuations, and expectations on general market and economic conditions.

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Buy/Addition to InStock Recommended List: We expect the Stock to Outperform the Market.

Hold/Addition to InStock Recommended List: We expect the Stock to be a Market Performer.

Sell/Removal from InStock Recommended List: We expect the Stock to Underperform the Market.

Ratings System in effect between 2/7/2002 and 6/12/2002: Strong Buy, Buy, Hold, Underperform, Sell.

Ratings System in effect prior to 2/7/2002: Buy, Moderate Buy, Hold, Underperform, Sell.

	Percentage of Rated Stocks Currently Assigned this Rating	Percentage of Rated Stocks with this Rating with which MWR has had an Investment Banking Relationship in the last 12 months
Buy	51%	9%
Hold	36%	4%
Sell	13%	0%

For Price Chart and Ratings History disclosures, please go to <http://www.mwrinc.com/ClientAccess/quotesresearch.html>, or to request information, please contact Sara E. Hasan, Research Assistant, (206) 664-8854, [mwr@mwrinc.com](mailto:mwr@mwrinc.com)

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**US Equity Research**  
J.P. Morgan Securities Inc.  
March 14, 2005

# Puget Energy

## Cutting Estimates and Downgrading to Neutral

### *Puget Energy*

**Neutral**

<i>Ticker</i>	<i>PSD</i>	<i>EPS</i>	<b>2004A</b>	<b>2005E (Old)</b>	<b>2005E (New)</b>	<b>2006E (Old)</b>	<b>2006E (New)</b>
<b>Price(03/11/05)</b>	\$22.25	<b>1Q (Mar)</b>	\$0.67	NA		NA	
<b>52-Wk.Range</b>	\$20.52-24.81	<b>2Q (Jun)</b>	\$0.16	NA		NA	
<b>Mkt.Cap(BN)</b>	\$2.22	<b>3Q (Sep)</b>	\$0.11	NA		NA	
<b>Fiscal Year</b>	Dec	<b>4Q (Dec)</b>	\$0.61	NA		NA	
<b>Shares O/S(MM)</b>	99.89	<b>FY</b>	\$1.60	\$1.50	\$1.40	\$1.70	\$1.55
<b>Div Yld</b>	4.49%	<b>P/E FY</b>	13.9	14.8	15.9	13.1	14.4

\*Official EPS estimates are rounded to the nearest \$0.05.

After working through recent EPS guidance, we are cutting our estimates and downgrading to Neutral from Overweight. We believe PSD may still deliver EPS growth as it invests in its rate base, but it appears that EPS power may not emerge for several quarters.

- We are cutting our 2005E EPS to \$1.40 from \$1.50 and our 2006E EPS to \$1.55 from \$1.70. We are also lowering our rating to Neutral from Overweight. We are downgrading the stock because although we believe Puget may ultimately deliver EPS growth to investors, it appears that regulatory lag as well as other factors may prevent EPS growth from emerging for the next several quarters.
- As we discussed in our note last week (3/10/05), we believe investors should excluded \$0.07 and \$0.05 in 2005 and 2006, respectively, from PSD's guidance for a regulatory disallowance. This moves PSD's 2005 guidance to \$1.37-1.47 and 2006 guidance to \$1.45-1.60. Based on our estimates, which fall within these ranges, the stock is trading at 14.4x 2006E EPS, which is about inline with the group.
- PSD yields slightly above the group average, but we estimate that it will earn an ROE of about 9% in 2005 and 2006 (versus 10.3% allowed), below most of its peers. While the above average yield should provide some support, given that the stock is trading inline with its peers and the company's struggle to deliver EPS growth we expect the shares to trade inline with the group for the next few quarters.
- We continue to believe that PSD's plan to invest in its utility can generate attractive EPS growth, but PSD must address the issues that are suppressing its EPS growth and ROE. In fact, if PSD is able to fix \$0.15 of regulatory lag in 2006, we believe the shares would be attractive, trading at 13.1x versus the group at 14.4x; however, we do not believe investors will get visibility on this for several quarters.

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### EPS Growth Hampered By Regulatory Lag, Among Other Factors

We present in Table 1 a summary calculation and analysis of Puget's EPS potential for 2005 and 2006 along with our estimates of its ROE for the same period. This analysis also reflects the company adding \$200 million to rate base in 2006 to reflect its investment in a wind farm project.

**Table 1: Reconciliation of Rate Base, Rate Base Additions and EPS Guidance**

EPS Reconciliation	2005E	2006E
Gas Rate Base (\$ Millions)	1,068	1,068
Electric Rate Base (\$ Millions)	2,545	2,545
Additions to Rate Base - Wind Projects (\$ Millions)	0	200
Total Rate Base (\$ Bn)	3,612	3,812
Equity Layer	43.00%	43.00%
Allowed ROE	10.30%	10.30%
Shares (millions)	100	104
<b>Projected Utility EPS</b>	<b>1.60</b>	<b>1.63</b>
Less: D&A Lag	-0.10	-0.08
Less: Incremental O&M	-0.05	-0.03
Less: Additional Debt Cost @ 7% for Wind Projects		-0.05
<b>JPMorgan Projected Ongoing EPS</b>	<b>1.45</b>	<b>1.47</b>
P/E	15.3x	15.2x
JPMorgan Projected Ongoing EPS Excluding Regulatory Lag		1.58
P/E		14.1x
Less: Tenaska Disallowance (we view this as non-recurring)	-0.07	-0.05
<b>EPS as Projected to Reconcile with PSD Guidance</b>	<b>1.38</b>	<b>1.42</b>
PSD Guidance Low-End	1.30	1.40
PSD Guidance High-End	1.40	1.55
Projected ROE Based on Guidance Mid-Point	8.7%	9.3%
Projected ROE Excluding Tenaska Disallowance	9.3%	9.3%

Source: JPMorgan estimates and Company Reports

### Valuation and Rating Analysis

We are downgrading Puget Energy to Neutral from Overweight because the company appears to be struggling with regulatory lag and other factors that are preventing its core utility EPS power from emerging. Our Overweight rating was based on what we expected to be an attractive EPS growth profile, aided in part by a constructive regulatory outcome of the company's recent electric rate case. We believe the recent electric rate case was resolved constructively; however, the company appears to be continuing to struggle to realize the full potential of its earnings power as established in its recent rate case. Longer-term, we believe Puget still has the potential to offer investors an attractive EPS growth profile; however, it appears that the company's struggle to earn its allowed ROE will prevent the potential EPS growth from investing in its utility from emerging for at least the next several quarters. We expect the company's above-average dividend to support the shares, and the shares are trading about in-line with the group average multiple of 14.5x 2006E EPS. Furthermore, if the company is able to address some of the issues masking its core utility earnings power, the shares appear attractively valued. For example, if the company is able to address \$0.15 of regulatory lag it is currently suffering by 2006, we estimate that the company could earn about \$1.70 in 2006, which would imply that the stock is trading at about 13.1x 2006E EPS, a significant discount to the group average 2006 multiple, especially given the company's above average yield. We believe this profile could ultimately prove attractive, but we expect the stock to trade inline with the group for the next several quarters because we do not believe visibility on potential EPS improvement will emerge over that time frame.

### Risks to Our Rating

Our downgrade to a Neutral rating for Puget shares is based on what we expect to be EPS dampened by regulatory lag and other factors for at least the next several quarters. This results in the company underearning its allowed ROE. If Puget continues to suffer from additional underearning pressure, or inability to add its planned utility investment to rate base, we would expect EPS, and thus the shares, to suffer. On the other hand, as we discussed above, if Puget is able to address its regulatory lag, we believe the shares appear attractive on a relative valuation. As we also discussed above, we expect visibility on this issue to take several quarters to emerge. If Puget is able to address its lag sooner rather than later, investors could get earlier visibility on higher EPS in 2006 and the shares could outperform.

### Companies Recommended in This Report

Puget Energy (PSD/\$22.25/Neutral)

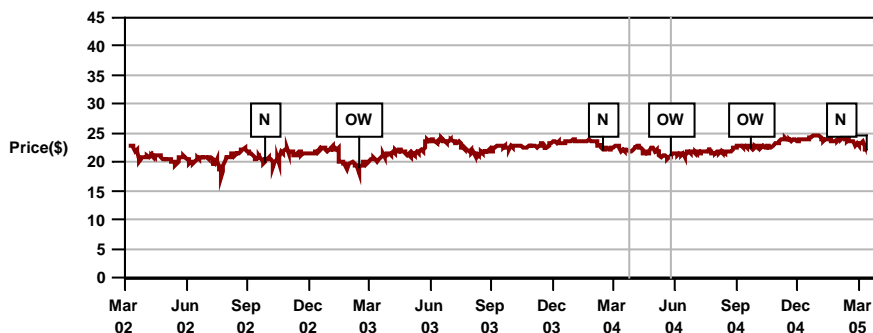
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Puget Energy (PSD) Price Chart



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.

Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.

JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

Ratings prior to Sept. 25, 2002: B = Buy, LTB = Long-Term Buy, MP = Market Performer, MU = Market Underperformer.

**Explanation of Ratings:** JPMorgan uses the following rating system: **Overweight** [Over the next six to twelve months, we expect this stock will outperform the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] **Neutral** [Over the next six to twelve months, we expect this stock will perform in line with

the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] **Underweight** [Over the next six to twelve months, we expect this stock will underperform the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] The analyst or analyst's team's coverage universe is the sector and/or country shown on the cover of each publication. Each analyst's coverage list, showing full coverage universe, is available on the analyst's page under the Research option on JPMorgan's website [www.morganmarkets.com](http://www.morganmarkets.com), accessible to JPMorgan's clients via password, or in the case of hard copy research or if no access to MorganMarkets, by calling this toll free number (1-800-477-0406).

Prior to September 25, 2002, our rating system was: Buy — we expect the stock to outperform the market by a minimum of 5% within an investment horizon of one year; Long-Term Buy — we believe the stock will outperform the market over the long run, but we lack the visibility of a catalyst for outperformance within a one-year investment horizon; Market Performer — the stock is expected to perform in line with the market; Market Underperformer — we expect the stock to underperform the market by a minimum of 5% within an investment horizon of one year.

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	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	39%	42%	19%
IB clients*	44%	44%	32%
JPM SI Equity Research Coverage	32%	49%	19%
IB clients*	64%	58%	43%

\*Percentage of investment banking clients in each rating category.

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# UBS Investment Research

## Puget Energy Inc.

Electric Utilities

**Rating** **Neutral 2**  
*Unchanged*
**Price target** **US\$21.00**  
*Prior: US\$23.00*
**Price** **US\$22.25**

RIC: PSD.N BBG: PSD US

**14 March 2005**
**Trading data**

52-wk. range	US\$24.73-20.54
Market cap.	US\$2.22bn
Shares o/s	99.7m
Free float	80%
Avg. daily volume ('000)	216
Avg. daily value (US\$m)	5.1

**Balance sheet data 12/05E**

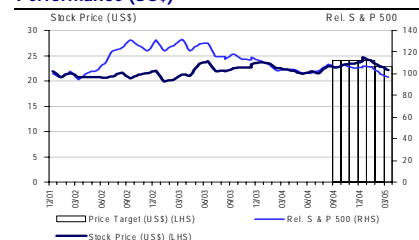
Shareholders' equity	US\$1.78bn
P/BV (UBS)	1.2x
Net cash (debt)	(US\$2.51bn)

**Forecast returns**

Forecast price appreciation	-5.6%
Forecast dividend yield	4.5%
Forecast stock return	-1.1%
Market return assumption	8.7%
Forecast excess return	-9.8%

**EPS (UBS, US\$)**

	12/05E		Cons.	12/04 Actual
	From	To		
Q1E	0.68	0.65	0.63	0.67
Q2E	0.16	0.15	0.14	0.16
Q3E	0.09	0.07	0.08	0.11
Q4E	0.58	0.55	0.58	0.61
12/05E	1.50	1.40	1.49	
12/06E	1.70	1.50	1.56	

**Performance (US\$)**


Source: UBS

[www.ubs.com/investmentresearch](http://www.ubs.com/investmentresearch)

## Outlook Murky, Lowering Price Target to \$21 from \$23

### Disappointing EPS Guidance for 2005 and 2006

Puget provided recurring EPS guidance of \$1.30-1.40 for 2005 and \$1.40-1.55 for 2006, respectively, both significantly below our estimates of \$1.50 and \$1.70. One major difference was the treatment of Infrastrux as discontinued ops (\$0.06). While mgmt did not spell out the details, we believe sizeable share dilution is implicit in the guidance for both the years.

### Lowering Estimates

We are lowering our recurring '05 EPS est. to \$1.40 from \$1.50, reflecting absence of Infrastrux earnings (0.06) and share dilution (\$0.04). We are also lowering '06 est. to \$1.50 from \$1.70 for the same reasons. We believe Puget will need to issue equity in both '05 and '06 to fund the two wind projects. We have also become more skeptical on the timing of recovery on the delivery capex.

### Normalized Earnings Power Getting Pushed Further Out

A combination of earnings lag on the delivery capex and repeated access to capital markets to fund rate base additions is depressing the true earnings power of the company. Several regulatory issues on the plate and a new Commission in Washington further reduce earnings visibility.

### Valuation: Lowering 12-month Price Target to \$21 from \$23

This reflects an updated DCF analysis based on revised cash flow assumptions and implies a 14.0x PE on our new 2006E EPS, roughly in-line with peers.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,188	2,386	-
EBIT	377	418	396	435	-
Net income (UBS)	110	155	146	167	-
EPS (UBS, US\$)	1.16	1.55	1.40	1.50	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	18.1	18.2	-
ROIC (EBIT) %	-	9.3	8.5	8.9	-
EV/EBITDA x	-	6.9	6.9	6.7	-
PE (UBS) x	-	14.6	15.9	14.8	-
Dividend yield %	-	4.4	4.5	4.5	-

Source: Company accounts, Thomson Financial, UBS estimates. UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$22.25 on 14 Mar 2005

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## Our View

Management held a conference call on Friday to discuss the 2005 and 2006 EPS guidance. While the numbers disappointed us by being much lower than our expectations, what disappointed us more was the lack of details in the call, especially regarding 2006 earnings. We understand that several regulatory issues on the plate, such as recovery of earnings lag on the delivery capex, recovery of the proposed wind additions and treatment of the Power Cost Adjustment (PCA) Mechanism post July 2006 make it difficult for management to handicap the outcomes. Nevertheless, we would have appreciated more visibility on the time line for the regulatory agenda as well as greater disclosure on the capex plans for 2005 and 2006 and sources of funding.

We are lowering our 12-month price target on PSD to \$21 from \$23 to reflect our updated cash flow assumptions in our DCF model. This implies a 14.0x PE on our 2006 EPS estimate, roughly in-line with the UBS Regulated Integrated Utilities Index average PE multiple. Our original above average EPS growth thesis on Puget has been diluted in the last few months given a lower than expected ROE and equity ratio outcome in the recently concluded general rate case and the revelation of earnings lag in the recovery of delivery capex. Also, a delay in the improvement in Puget's leverage necessitates equity issuances to finance rate base additions; thus, diluting the potential earnings impact. Our view on the stock is further tempered by several key risks that face the company, including regulatory risks and Least Cost Plan execution risks.

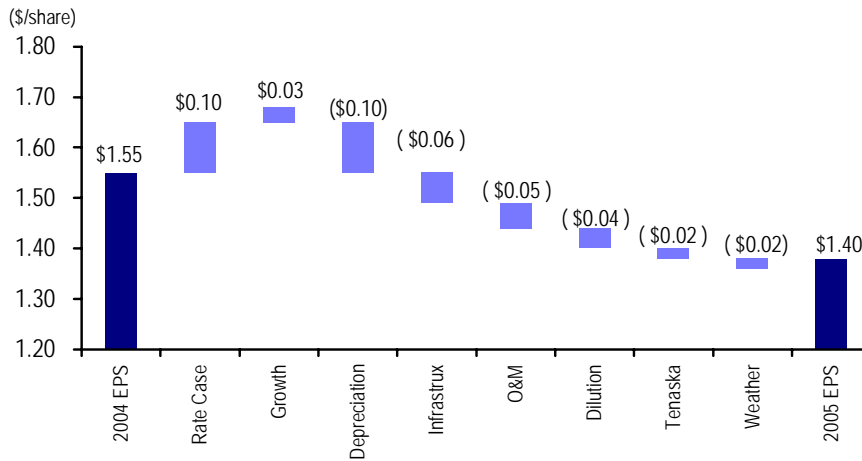
Price movement to our new \$21 price target – when combined with the current \$1/share annual dividend (or 4.5% yield) – suggests a negative 1.1% 12-month total return potential. We maintain our Neutral 2 rating.

## Lowering 2005 and 2006 EPS Estimates

We are lowering our recurring 2005 and 2006 EPS estimates to \$1.40 and \$1.50, from \$1.50 and \$1.70, respectively. Charts 1 and 2 illustrate the factors impacting our estimates. We would add here that we have limited confidence in our 2006 EPS estimate since there are several regulatory unknowns as aforementioned.

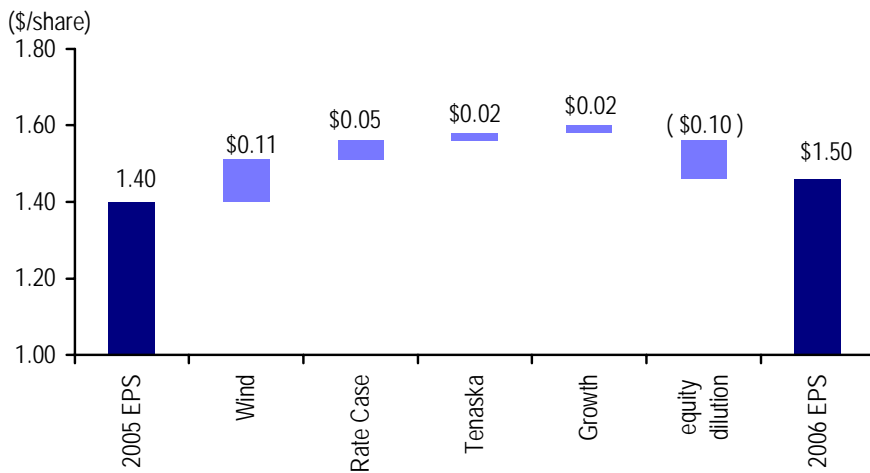


**Chart 1: Factors Affecting 2005E EPS Compared With 2004 EPS**



Source: UBS estimates

**Chart 2: Factors Affecting 2006E EPS Compared With 2005E EPS**



Source: UBS estimates

## ■ Puget Energy Inc.

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. InfrastruX provides infrastructure construction services to the electric and gas utility industries.

## ■ Statement of Risk

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.

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UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	36%	32%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	53%	35%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	29%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 31 December 2004.

### KEY DEFINITIONS

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

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**Rating/Return Divergence (RRD)** This qualifier is automatically appended to the rating when stock price movement has caused the prevailing rating to differ from that which would be assigned according to the rating system and will be removed when there is no longer a divergence, either through market movement or analyst intervention.

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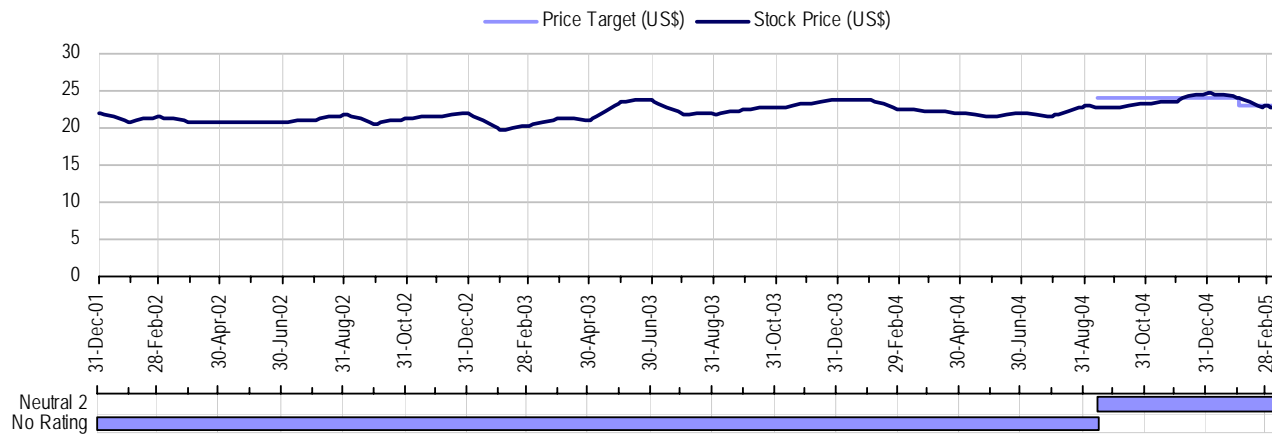
Company Name	Reuters	Rating	Price
Puget Energy Inc. <sup>4,6a,6b,6c,7,16</sup>	PSD.N	Neutral 2	US\$22.25

Price(s) as of 11 March 2005. Source: UBS.

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**Puget Energy Inc. (US\$)**



Source: UBS; as of 11 March 2005.

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14 March 2005

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# Puget Energy Inc.

On a Treadmill?

NEUTRAL

Reason for Report: Disappointing 2005/2006 Guidance

Volatility Risk:  
MEDIUM

Company

**PSD; \$22.25; B-2-7**EPS (Dec): 2004A \$1.60; 2005E \$1.30; 2006E \$1.40  
P/E (Dec): 2004A 13.9x; 2005E 17.1x; 2006E 15.9xGAAP EPS (Dec): 2004A \$0.55; 2005E \$1.30; 2006E \$1.40  
GAAP P/E (Dec): 2004A 40.5x; 2005E 17.1x; 2006E 15.9x**Event**

**Last Friday, PSD offered its outlook for 2005.** Management announced that it expects to achieve EPS of \$1.30-\$1.40 per share in 2005 and \$1.40-\$1.55 in 2006.

**Analysis**

**We'd expected 05 EPS closer to the allowed rate of return.** The PCA tracker is maxed, and with the general revenue increase of \$83M, we were looking for a target range of somewhere in the \$1.60/sh range this year, roughly equivalent to the "theoretical" earning power PSD discussed based on its allowed 10.3% ROE, rate base and capital structure.

**Costs are going up faster than they can be recovered.** First and foremost, costs associated with energy delivery infrastructure are rising fast. PSD expects energy delivery capex of about \$380M in 2005 and another \$400M in 2006, driving higher but unrecovered DD&A. Much of this capex (about 2/3) is driven by system upgrades and remediation, so O&M is going up sharply as well. Second, the divestiture of InfrastruX will impact earnings by at least \$0.06, although we weren't including that income.

**Why weren't these costs included in the recent rate case?** Because a historical test year was used instead of a forecasted test year, *the lag in recouping these energy delivery infrastructure costs will reduce earnings by ~\$0.15/sh this year...about \$0.10/sh of additional D&A and \$0.05/sh of additional O&M.* Finally, the ongoing drag from Tenaska disallowance continues to cost \$0.06 to \$0.07.

**Recommendation**

**We are reducing our 2005 EPS estimate from \$1.60/sh to \$1.30/sh.** We are initiating our 2006 estimate at \$1.40/sh to reflect a continuation of the higher cost environment. We'll stay at the low end of management's forecasts, and until the company is able to better manage or recover these costs, we believe PSD will continue to under-earn...and likely under-perform.

**PSD seems to be on a regulatory treadmill.** With backward-looking ratemaking and rising costs, this will be a tough cycle to break. And, the combination of new regulators and high system upgrade costs gives us some concern about the likely "pancaking" of rate cases that lies ahead. The 4.5% yield provides some downside support, but we believe upside in PSD shares is likely to be limited for some time.

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Refer to important disclosures on pages 3 to 4. Analyst Certification on page 2.

## Analyst Certification

I, Sam Brothwell, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

**Table 1: PSD Financial Outlook 2004A - 2006E**

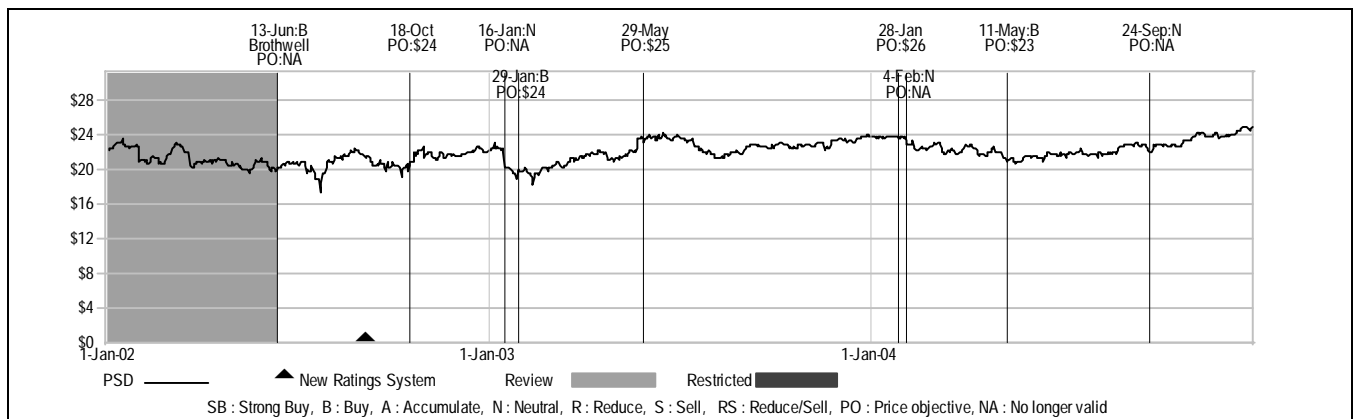
	2004A	2005E	2006E
Total Revenues	2,568.8	2,199.2	2,225.6
Expenses			
Purchased Electricity	723.6	738.0	749.1
Purchased Gas	408.5	389.2	391.7
O&M--Utility	291.2	308.2	314.4
O&M Other	322.5	2.4	2.5
DD&A--Utility	246.8	251.8	255.6
Conservation & Amortization	22.7	23.0	23.0
Other Taxes	222.0	197.9	197.9
Other	(94.2)	(90.5)	(90.0)
Total Expenses	2,143.1	1,820.1	1,844.2
Operating Income	425.7	379.1	381.4
Other Income	4.3	3.0	3.0
Minority Interest	7.1	0.0	0.0
Interest Expense	173.1	167.8	151.5
Pretax Income	249.9	214.4	232.9
Income Taxes	90.2	81.5	88.5
Equity Earnings	0.0	0.0	0.0
Income from Cont Operations	\$159.7	\$132.9	\$144.4
Cum. Effect of Acctg Change (133)			
Income Tax Rate (%)	36.1%	38.0%	38.0%
Discontinued Operations			
Income	\$0.00	\$0.00	\$0.00
Gain (Loss) From Disposal	0.00	0.00	0.00
Total	0.00	0.00	0.00
Non-Recurring Items - Net	(104.70)	(6.11)	0.00
Net Income	55.00	126.80	144.42
Preferred Dividends	0.00	0.00	0.00
Net Available to Common	\$55.00	\$126.80	\$144.42
Avg. Common Shares and Dilutive Common Stock Equivalents Outstanding (mm)	99.9	101.91	102.93
Recurring EPS	\$1.60	\$1.30	\$1.40
Reported EPS	0.55	1.24	1.40
Discontinued Operations	0.00	0.06	0.00
Total EPS	\$0.55	\$1.24	\$1.40

Source: Merrill Lynch & Company Reports



## Important Disclosures

PSD Price Chart



From 8 Dec. 2001 to 6 Sep. 2002, the Investment Opinion System included: Strong Buy, Buy, Neutral, and Reduce/Sell. On 6 Sep. 2002, Strong Buy and Buy ratings became Buy, and Reduce/Sell became Sell. Any exceptions to these rating revisions are reflected in the chart. All price objectives for Neutral and Sell rated securities established before 6 Sep. 2002 were eliminated as of that date. The current Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark Grey shading indicates the security is restricted with the opinion suspended. Light Grey shading indicates the security is under review with the opinion withdrawn.



Investment Rating Distribution: Energy Group (as of 31 December 2004)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	47.06%	Buy	28	38.89%
Neutral	76	49.67%	Neutral	29	38.16%
Sell	5	3.27%	Sell	0	0.00%
Investment Rating Distribution: Global Group (as of 31 December 2004)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1054	40.45%	Buy	383	36.34%
Neutral	1339	51.38%	Neutral	382	28.53%
Sell	213	8.17%	Sell	43	20.19%

\* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

**FUNDAMENTAL EQUITY OPINION KEY:** Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. **VOLATILITY RISK RATINGS**, indicators of potential price fluctuation, are: A - Low, B - Medium, and C - High. **INVESTMENT RATINGS**, indicators of expected total return (price appreciation plus yield) within the 12-month period from the date of the initial rating, are: 1 - Buy (10% or more for Low and Medium Volatility Risk Securities - 20% or more for High Volatility Risk securities); 2 - Neutral (0-10% for Low and Medium Volatility Risk securities - 0-20% for High Volatility Risk securities); 3 - Sell (negative return); and 6 - No Rating. **INCOME RATINGS**, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure); 8 - same/lower (dividend not considered to be secure); and 9 - pays no cash dividend.

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MLPF&S or an affiliate expects to receive or intends to seek compensation for investment banking services from this company within the next three months: Puget Energy.

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MARCH 14, 2005

UTILITIES

# Puget Energy, Inc.

NYSE - PSD

## Management Outlines Forward Guidance Due to Recent General Rate Decision Lowering Our FY05 EPS Estimate

 ANALYST OPINION: **SELL**

### PRIMARY STOCK STATISTICS

FY End	Dec
52-Week Range	\$25-\$21
Market Cap (billion)	\$2.21
TTM Revenue (billion)	\$2.57
Shares Outstanding (million)	99.8
Book Value	\$15.96
Dividend/Yield	\$1.00/4.5%
Est. Sec. EPS Grth Rate	5%

PRICE: \$22.14

PRICE TARGET: NA

### EARNINGS ESTIMATES

Current Quarter

FY03A

FY04A

FY05E

### PRIOR

-

-

\$1.66

### CURRENT

-

\$1.22

\$1.26

\$1.35

### P/E

-

18.1x

17.8x

16.4x

### KEY POINTS

- Management outlined its forward EPS guidance incorporating the implications of the recent general rate case decision handed down by the WUTC. The Company expects the core utility to earn \$1.30-\$1.40 in FY05 and \$1.40-\$1.55 in FY06. (Core utility EPS in FY04 was \$1.26.)
- Given the current rate base (\$3.6 billion) and the regulatory return on equity set at 10.3% on a 43% equity capitalization, the core utility theoretically could generate EPS of \$1.60 but various factors will reduce it, including the Tenaska disallowance and higher than test year expense for both depreciation and operations and maintenance (O&M) (all of which will likely continue over the next couple years).
- Management indicated that the Company will add 500-550MW of wind generation capacity by 2006 (at a projected capex of \$500 million). The first 150MW project was announced on Friday and will likely be equity financed.
- We are reducing our FY05 EPS estimate to \$1.35 (from \$1.66). Nothing in the updated guidance changes our view on the stock so we maintain our SELL rating. With a forward P/E multiple above 16x (based on current price) and equity dilution likely over the next two years to acquire/build captive generation assets, we see little holding the stock price up but the current dividend.

### SUMMARY AND STOCK OPINION

On Friday, Puget Energy's management discussed the ramifications of the recent Washington Utilities and Transportation Commission's decision regarding its general rate case filing. As a result of the decision, management is guiding FY05 EPS for the core utility at \$1.30-\$1.40, lower than previous expectations. Furthermore, preliminary EPS guidance for FY06 was promulgated in the \$1.40-\$1.55 range. We are reducing our FY05 EPS estimate to \$1.35 but are not yet committing to a FY06 estimate.

(Continued)

This forward guidance appears to confirm our decision to downgrade the stock to SELL last month. While we are reasonably confident that trends are now beginning to turnaround for the Company on the regulatory and business front, the lower forward earnings guidance removes one of the remaining legs under the current stock price in our opinion. Trading at over 16x our FY05 EPS estimate and 15x the midrange of management's FY06 EPS guidance, there is little holding up the stock price but the current dividend yield (4.5%). With equity dilution likely as the Company builds/acquires additional generation assets over the next two years, we see the Company with little financial flexibility should interest rates continue to rise.

Puget Energy, Inc. is one of Washington state's largest utility companies. Through its subsidiary, Puget Sound Energy, it provides electricity to more than 940,000 customers and provides natural gas to more than 600,000 in western Washington. The company owns some fossil-fueled and hydroelectric plants and its InfrastruX Group specializes in energy management and infrastructure construction services. Headquarters: Bellevue, WA

**S&P 500: 1200.82**

**REQUIRED DISCLOSURES**

The analyst or a member of the analyst’s household has beneficial ownership in the securities of Puget Energy, Inc. in the form of a long position in such securities.

**ANALYST CERTIFICATION**

By issuing this research report, each Ragen MacKenzie analyst whose name appears on the front page of this research report hereby certifies that: (i) the recommendations and opinions expressed in the research report accurately reflect the research analyst’s personal views about any and all of the subject securities or issuers discussed herein and (ii) no part of the research analyst’s compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in the research report.

**PRICE TARGET VALUATION METHODOLOGY AND RISKS**

The methods used to determine the price target are generally based on a multiple of earnings, cash flow, revenue and/or historical and relative valuation multiples. Risks that could impede achievement of our price target include, but are not limited to, changes in economic and industry conditions, consumer and business spending patterns, as well as geo-political risks. When a price target is used, please refer to the Valuation and Risks section in the body of the report for additional discussion on the specific valuation methodology and related risk factors as they pertain to this analyst’s investment thesis.

**RATING SYSTEM**

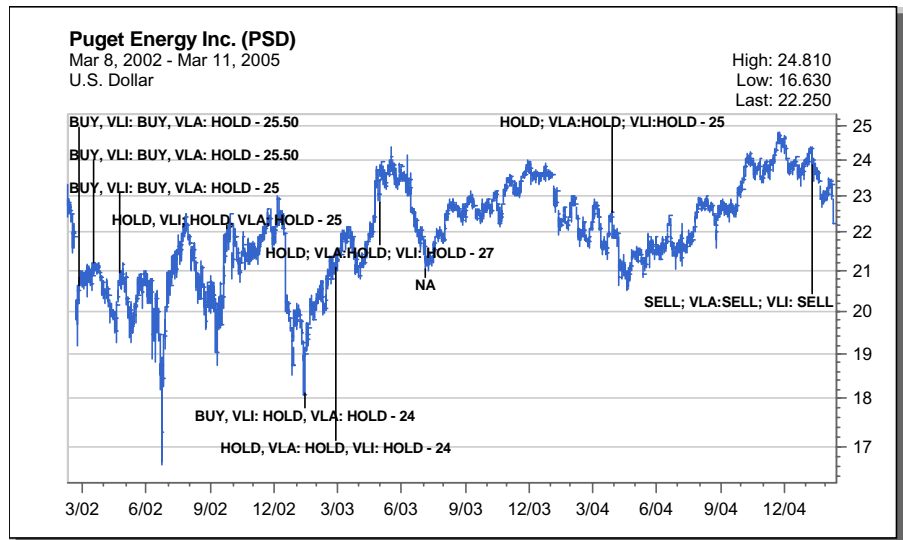
**BUY** – Immediate purchase is recommended; the stock is expected to outperform the general market over the next 12-18 months.  
**HOLD** – Holding the stock is recommended. The stock has moved out of our preferred buying range, but there is further upside to the share price; or stated objectives at the time of purchase have changed and share appreciation may take another 6-12 months.  
**SELL** – The stock has reached the stated price objective and appreciation has been achieved; or certain company fundamentals have changed which warrant investors selling the stock to avoid price decline.

**RATINGS ALLOCATIONS**

Rating	% of covered companies with this rating	% for which IB Services have been provided
<i>Analyst Coverage</i>		
BUY	20%	0%
HOLD	73%	8%
SELL	8%	0%
<i>Value Recommended List—Appreciation</i>		
BUY	22%	0%
HOLD	61%	9%
SELL	17%	0%
<i>Value Recommended List—Income</i>		
BUY	43%	33%
HOLD	43%	33%
SELL	14%	0%
<i>Growth Recommended List</i>		
BUY	14%	0%
HOLD	71%	0%
SELL	14%	0%

Updated on 01/03/2005

**PRICE HISTORY**



The price targets indicated in the chart above may be adjusted for stock splits. Where the price target was originally given as a range, the midpoint of the range has been used. Until July 8, 2002, Ragen MacKenzie used the following system for analyst ratings: Strong Buy (SB), Buy, Market Perform (MP), Underperform, Sell. The current rating system, explained above, has been in effect since July 9, 2002.

**OTHER DISCLOSURES**

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**PUGET ENERGY, INC.**

PSD – NYSE

April 25, 2005

**Rating:****NEUTRAL****Price:** (4/22/05) \$21.58**Price Targets:**

12-18 month: \$23

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

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**1Q'05 Earnings Preview and Other Comments.**

Puget Energy reports 1Q'05 results after the market close on Thursday, April 28, and holds a conference call on Friday, April 29, at 7:00 a.m. PDT. We have been forecasting EPS of \$0.62 vs. \$0.67, with utility results down nearly 10%, due in part to the impacts of mild 1Q'05 temperatures.

As noted in our *Utility Monthly* of April 5, 2005, 1Q'05 cooling degree days in Seattle were 7% lower than normal and 2% lower than 1Q'04.

The 15% quarterly earnings decline reported by Cascade Natural Gas (CGC - \$18.63) for the period ended March 31, 2005 does not bode well for the soon-to-be-reported 1Q'05 results of neighboring Puget Energy. Tepid results by Cascade suggest that mild 1Q'05 temperatures and reduced per customer consumption, due to conservation efforts spurred by higher natural gas prices, also likely reduced the gas and electric consumption of Puget's utility customers.

Three observations mitigate possible fears of a major earnings miss. First is the fact the company has not pre-announced 1Q'05 earnings. Second, management initiated 2005 EPS guidance on March 10, after most of the quarter was already completed and the weather impacts were already known in good part. That guidance was an annual EPS range of \$1.30-\$1.40. Puget, however, did not provide quarterly guidance. Third, with the share price off 12% since year-end 2004, much of the concerns about the impacts of milder winter weather are likely already factored into the stock. (We believe the recent decline in share price is more a factor of reduced earnings expectations, following the decision of Puget's recent rate case, than of weather-related issues. See our *Research Bulletin* of February 22, 2005.)

Our 2005 forecast of \$1.42 is slightly above the company's guidance range because it includes a contribution of \$0.04 per share from InfrastruX, the company's utility services business. Puget anticipates selling or monetizing InfrastruX in 2005, and has classified it in discontinued operations. Any 2005 earnings contribution from InfrastruX has been excluded from management's guidance range, but has not yet been removed from our forecast. (We have not revised our forecast for InfrastruX being accounted for as a discontinued operation, since, up until this week, the company had not provided the historical annual restatements. However, lacking the quarterly restatements, we haven't yet attempted to recast our earnings model.)

Also, earlier this week, Puget filed a shelf registration of \$850 million in senior secured debt and common stock. Our 2006 EPS for Puget has assumed that the company will offer approximately 5 million common shares at year-end 2005. The company needs the stock and bond financings to carry out an ambitious capital expenditure plan and to increase the equity ratio to a target level of 43%.

**RESEARCH NOTE**

Please refer to pages 2-3 of this report for detailed disclosure and certification information.

D.A. Davidson & Co.

Two Centerpointe Drive, Suite 400 • Lake Oswego, Oregon 97035 • (503) 603-3000 • (800) 755-7848 • [www.davidson.com](http://www.davidson.com)

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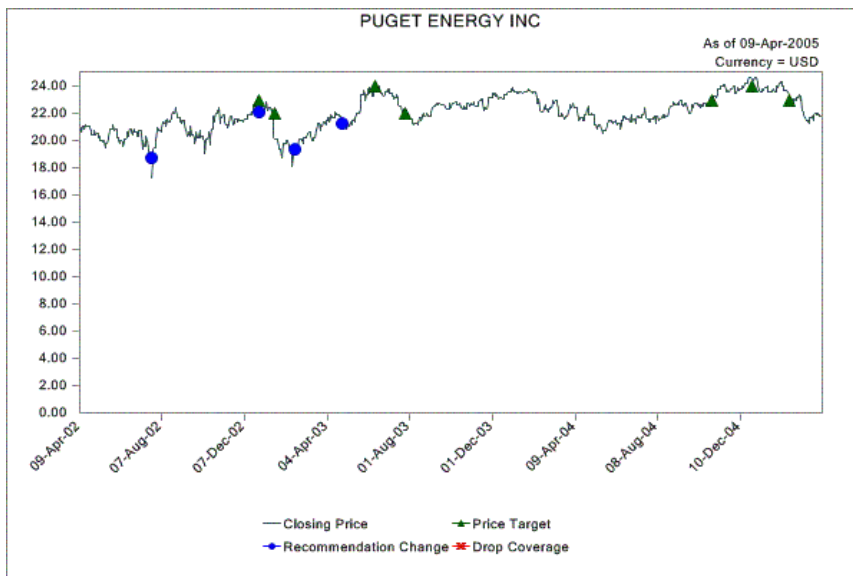
## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 3/31/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 40%	Neutral 50%	Underperform 10%
Corresponding Private Client Research Ratings and Distribution	Buy, Core/Buy 65%	Hold, Core/Hold 35%	Avoid 0%
Distribution of Combined Ratings	45%	47%	8%

### Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.

Institutional Coverage	8%	12%	7%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	6%	10%	7%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
Strong Buy, Buy, Neutral, Underperform

PUGET ENERGY INC					
Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
22-Jul-2002	18.73	BUY	24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

**D.A. Davidson & Co.**

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

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**US Equity Research**  
J.P. Morgan Securities Inc.  
April 29, 2005

# Puget Energy

## 1Q05 Result Establishes Solid Foundation for 2005

### *Puget Energy*

**Neutral**

<i>Ticker</i>	<i>PSD</i>	<i>EPS</i>	<b>2004A</b>	<b>2005E</b>	<b>2006E</b>
<b>Price(04/29/05)</b>	\$21.37	<b>1Q (Mar)</b>	\$0.67	\$0.70A	
<b>52-Wk.Range</b>	\$20.52-24.81	<b>2Q (Jun)</b>	\$0.16		
<b>Mkt.Cap(BN)</b>	\$2.13	<b>3Q (Sep)</b>	\$0.11		
<b>Fiscal Year</b>	Dec	<b>4Q (Dec)</b>	\$0.61		
<b>Shares O/S(MM)</b>	99.89	<b>FY</b>	\$1.60	\$1.40	\$1.55
<b>Div Yld</b>	4.66%	<b>P/E FY</b>	13.4	15.3	13.8

\*Official EPS estimates are rounded to the nearest \$0.05.

PSD reported 1Q05 EPS from continuing operations of \$0.70, ahead of Street expectations, but inline with our estimate. Management reiterated 2005 guidance of \$1.30-1.40 per share from continuing operations. We reiterate our Neutral recommendation on the shares.

**US Electric Utilities:**

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- PSD reported 1Q05 EPS from continuing operations of \$0.70. We have removed the net benefit of \$0.02 per share related nonrecurring regulatory items. Lower interest expense, lower storm costs, and rate relief for a portion of the quarter were largely offset by higher D&A and O&M costs. As a winter peaking utility, 1Q and 4Q typically contribute about 80% of full year EPS, and thus, this is a solid start for PSD.
- Construction on the 160MW Hopkins Ridge wind project is underway with an expected completion by year end. The company's second wind project, Wild Horse, is 200MW and should be completed by the end of 2006. The company will soon submit its 2005 Least Cost Plan with the Washington Utility and Transportation Commission, and an RFP is forthcoming later this year to evaluate another round of resource additions.
- As we discussed in our previous note (3/10/05), we believe investors should excluded \$0.07 and \$0.05 in 2005 and 2006, respectively, from PSD's guidance for a regulatory disallowance. This moves PSD's 2005 guidance to \$1.37-1.47 and 2006 guidance to \$1.45-1.60. Based on our estimates, which fall within these ranges, the stock is trading at 13.8x 2006E EPS, which is just below the group at 14.5x.

**Valuation and Rating Analysis**

We downgraded Puget Energy to Neutral in March as the company appears to be struggling with regulatory lag and other factors that are preventing its core utility EPS

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power from emerging. Previously our thesis was based on what we expected to be an attractive EPS growth profile, aided in part by a constructive regulatory outcome of the company's recent electric rate case. We believe the recent electric rate case was resolved constructively; however, the company appears to be continuing to struggle to realize the full potential of its earnings power as established in its recent rate case. Longer-term, we believe Puget still has the potential to offer investors an attractive EPS growth profile; however, it appears that the company's struggle to earn its allowed ROE will prevent the potential EPS growth from investing in its utility from emerging for at least the next several quarters. We expect the company's above-average dividend to support the shares, and the shares are trading just below the group average multiple of 14.5x 2006E EPS. Furthermore, if the company is able to address some of the issues masking its core utility earnings power, the shares appear attractively valued. For example, if the company is able to address \$0.15 of regulatory lag it is currently suffering by 2006, we estimate that the company could earn about \$1.70 in 2006, which would imply that the stock is trading at about 12.6x 2006E EPS, a significant discount to the group average 2006 multiple, especially given the company's above average yield. We believe this profile could ultimately prove attractive, but we expect the stock to trade inline with the group for the next several quarters because we do not believe visibility on potential EPS improvement will emerge over that time frame.

### **Risks to Our Rating**

Our Neutral rating on Puget shares is based on what we expect to be EPS dampened by regulatory lag and other factors for at least the next several quarters. This results in the company underearning its allowed ROE. If Puget continues to suffer from additional underearning pressure, or inability to add its planned utility investment to rate base, we would expect EPS, and thus the shares, to suffer. On the other hand, as we discussed above, if Puget is able to address its regulatory lag, we believe the shares appear attractive on a relative valuation. As we also discussed above, we expect visibility on this issue to take several quarters to emerge. If Puget is able to address its lag sooner rather than later, investors could get earlier visibility on higher EPS in 2006 and the shares could outperform.

### **Companies Recommended in This Report**

Puget Energy (PSD/\$21.37/Neutral)

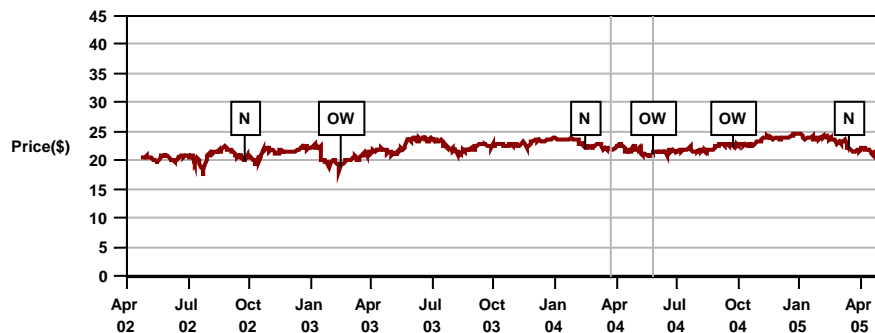
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Puget Energy (PSD) Price Chart



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.

Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.

JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

Ratings prior to Sept. 25, 2002: B = Buy, LTB = Long-Term Buy, MP = Market Performer, MU = Market Underperformer.

**Explanation of Ratings:** JPMorgan uses the following rating system: **Overweight** [Over the next six to twelve months, we expect this stock will outperform the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] **Neutral** [Over the next six to twelve months, we expect this stock will perform in line with the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] **Underweight** [Over the next six to twelve months, we expect this stock will underperform the average total return of the stocks in the analyst's (or the analyst's team's) coverage universe.] The analyst or analyst's team's coverage universe is the sector and/or country shown on the cover of each publication. Each analyst's coverage list, showing full coverage universe, is available on the analyst's page under the Research option on JPMorgan's website [www.morganmarkets.com](http://www.morganmarkets.com), accessible to JPMorgan's clients via password, or in the case of hard copy research or if no access to MorganMarkets, by calling this toll free number (1-800-477-0406).

Prior to September 25, 2002, our rating system was: Buy — we expect the stock to outperform the market by a minimum of 5% within an investment horizon of one year; Long-Term Buy — we believe the stock will outperform the market over the long run, but we lack the visibility of a catalyst for outperformance within a one-year investment horizon; Market Performer — the stock is expected to perform in line with the market; Market Underperformer — we expect the stock to underperform the market by a minimum of 5% within an investment horizon of one year.

**JPMorgan Equity Research Ratings Distribution, as of March 31, 2005**

	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	39%	42%	18%
IB clients*	47%	47%	37%
JPMSI Equity Research Coverage	34%	48%	18%
IB clients*	66%	59%	45%

\*Percentage of investment banking clients in each rating category.

For purposes only of NASD/NYSE ratings distribution rules, our Overweight rating falls into a buy rating category; our Neutral rating falls into a hold rating category; and our Underweight rating falls into a sell rating category.

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Americas

Electric Utilities

**Rating** **Neutral 2**  
**Unchanged**

**Price target** **US\$21.00**  
**Unchanged**

**Price** **US\$21.20**

RIC: PSD.N BBG: PSD US

**29 April 2005**

**Trading data**

52-wk. range	US\$24.73-20.54
Market cap.	US\$2.11bn
Shares o/s	99.7m
Free float	80%
Avg. daily volume ('000)	320
Avg. daily value (US\$m)	7.1

**Balance sheet data 12/05E**

Shareholders' equity	US\$1.78bn
P/BV (UBS)	1.2x
Net cash (debt)	(US\$2.51bn)

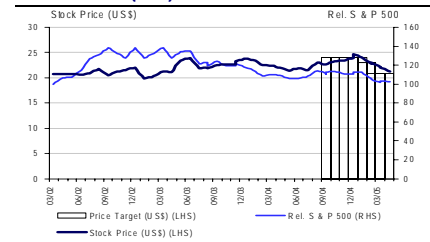
**Forecast returns**

Forecast price appreciation	-0.9%
Forecast dividend yield	4.7%
Forecast stock return	+3.8%
Market return assumption	8.6%
Forecast excess return	-4.8%

**EPS (UBS, US\$)**

	12/05E		12/04 Actual
	From	To	
Q1	0.65	0.65	0.64
Q2E	0.15	0.15	0.14
Q3E	0.07	0.07	0.07
Q4E	0.55	0.55	0.57
12/05E	1.40	1.40	1.37
12/06E	1.50	1.50	1.49

**Performance (US\$)**



Source: UBS  
[www.ubs.com/investmentresearch](http://www.ubs.com/investmentresearch)

**This report has been prepared by UBS Securities LLC**

**UBS Investment Research**

**Puget Energy Inc.**

**In-Line Results, Maintaining Estimates**

■ **Results in-line with expectations**

Puget realized recurring 1Q EPS of \$0.68, modestly higher than \$0.67 realized in 1Q04. The results were \$0.03 above our est. of \$0.65 and \$0.04 above the Street consensus of \$0.64. Please note, we clean the reported \$0.71 EPS for a \$6 million pre-tax benefit due to reversal of Tenaska disallowance (which translates into roughly \$0.04) and a loss at Infrastrux of \$0.01.

■ **Maintaining EPS estimates**

Management reiterated Puget's recurring EPS guidance of \$1.30 – 1.40 for 2005 and \$1.40 – 1.55 for 2006, respectively. We are maintaining our 2005 and 2006 EPS estimates at \$1.40 and \$1.50, respectively.

■ **Busy regulatory calendar ahead**

While 1Q results were in-line with our ests., our outlook on the stock is tempered by several regulatory issues on the plate, such as recovery of the earnings lag on the delivery capex, recovery of the proposed wind additions, and treatment of the Power Cost Adjustment (PCA) Mechanism post July 2006.

■ **Valuation: Maintaining price target at \$21**

Our price target is derived using a DCF analysis. This implies a 14.0x PE on our recurring 2006 EPS or in-line with peers, which we believe to be appropriate given our expectation that regulatory uncertainty will offset Puget's above average earnings growth potential.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,188	2,386	-
EBIT	377	418	396	435	-
Net income (UBS)	110	155	146	167	-
EPS (UBS, US\$)	1.16	1.55	1.40	1.50	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	18.1	18.2	-
ROIC (EBIT) %	-	9.3	8.5	8.9	-
EV/EBITDA x	-	6.9	6.7	6.5	-
PE (UBS) x	-	14.6	15.1	14.1	-
Dividend yield %	-	4.4	4.7	4.7	-

Source: Company accounts, Thomson Financial, UBS estimates. UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$21.20 on 28 Apr 2005 15:29 EDT

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**ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 5**

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## Earnings Summary

Puget realized a 1% increase in recurring 1Q diluted EPS, to \$0.68 from \$0.67 in 1Q04. The results were \$0.03 above our estimate of \$0.65 and \$0.04 above the Street consensus estimate of \$0.64. Please note, we clean the reported 1Q05 EPS of \$0.71 for a \$6 million pre-tax benefit due to reversal of Tenaska disallowance (which translates to roughly \$0.04) and a loss at Infrastrux of \$0.01, which is reflected as discontinued operations. Earnings for the quarter were driven by an increase in the electric margin and a decrease in interest expense at the utility. Offsets were higher depreciation and amortization over the quarter.

Management reiterated Puget's recurring EPS guidance at \$1.30 –1.40 for 2005 and \$1.40 – 1.55 for 2006, respectively. Puget expects its 2005 earnings to be minimally impacted by power costs falling outside the baseline as it reached its power cost adjustment (PCA) capacity last year. Further, 99% of the increase in variable power costs will be absorbed by customers until mid-2006.

**S-3 Registration:** On April 19<sup>th</sup>, Puget filed an S-3 registration allowing the company to periodically sell up to \$850 million in senior debt and common stock. The company intends to use the proceeds for general corporate purposes including debt repayment, capital expenditures, investments in subsidiaries and working capital. We are not surprised by the measure, as similar to what we have commented in the past, we expect Puget to issue equity in the near future to partially fund the rate base additions. That said, management noted in today's conference call that it does not plan to issue equity in 2005 to fund its current year capex plans.

**Wind Update:** Management provided an update with respect to the two recently announced wind power projects – the 150 MW Hopkins Ridge project and the 160 MW Wild Horse project. Construction of the Hopkins Ridge project has begun and the plant is expected to be operational by December 2005. The Wild Horse project is currently moving through a permitting process and is expected to be completed by the end of 2006.

## Our View

While the first quarter results were in-line with our estimates, our outlook on the stock remains clouded due to regulatory uncertainty. There are several regulatory issues on the plate, such as recovery of the earnings lag on the delivery capex, recovery of the proposed wind additions and treatment of the Power Cost Adjustment (PCA) Mechanism post July 2006. At the same time, we acknowledge the strides the company has taken to right size itself including leverage reduction to 60% at the end of 2004 from 70% in 2003 and the progress on its Least Cost Plan (LCP) with the addition of two wind projects.

## Maintaining Estimates

We are maintaining our recurring 2005 EPS estimate at \$1.40, which compares with the First Call consensus estimate of \$1.37 (reflecting a range of \$1.30 – 1.42). We are also maintaining our 2006 EPS estimate at \$1.50. This compares with the Street consensus estimate of \$1.49 (reflecting a range of \$1.40 – 1.55).

## Maintaining Price Target at \$21

Our 12-month price target of \$21 per share is derived using a DCF analysis. This implies a 14.0x PE on our recurring 2006 EPS or in-line with peers, which we believe to be appropriate given our expectation that regulatory uncertainty will offset Puget's above-average earnings growth potential.

Price movement to \$21 per share – when combined with the current \$1.00/share annual dividend (or 4.7% yield) – suggests a 3.8% total return potential.

## Key 1Q05 EPS Drivers

Puget Sound Energy (PSE), the utility, realized recurring 1Q05 EPS of \$0.68 versus \$0.67 in 1Q04. Results were driven by higher electric margin due to contribution from the Fredrickson plant and the March 4, 2005, base rate increase, partially offset by warmer weather (+\$0.01). In early March this year, Washington Utilities and Transportation Commission (WUTC) granted PSE an annualized general rate increase of roughly \$58 million for its electric customers and roughly \$26 million for its natural gas customers. The utility's margins in the quarter were slightly hurt due to warmer weather. PSE reported 3.5% lower gas sales volumes due to fewer year-over-year heating-degree days. However, the strength in customer growth continued with the electric and gas customers increasing by 2% and 3%, respectively, over 1Q04. Other positives in the quarter include lower interest and storm expenses (+\$0.02). The reduction in interest expense resulted from initiatives to reduce debt and refinance higher cost securities. These positives were partially offset by increased depreciation and amortization expense (-\$0.02).

We note that since PSE operates in a winter peaking region of the nation, it has already realized over half of its low-end guidance range. We will expect the second and especially third quarter to be lower earnings periods. We believe the company's pre-guidance range already accounted for the weaker weather in the first quarter.

## ■ Puget Energy Inc.

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. InfrastruX provides infrastructure construction services to the electric and gas utility industries.

## ■ Statement of Risk

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.



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UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	37%	30%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	52%	32%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	25%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 31 March 2005.

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**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

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Companies mentioned

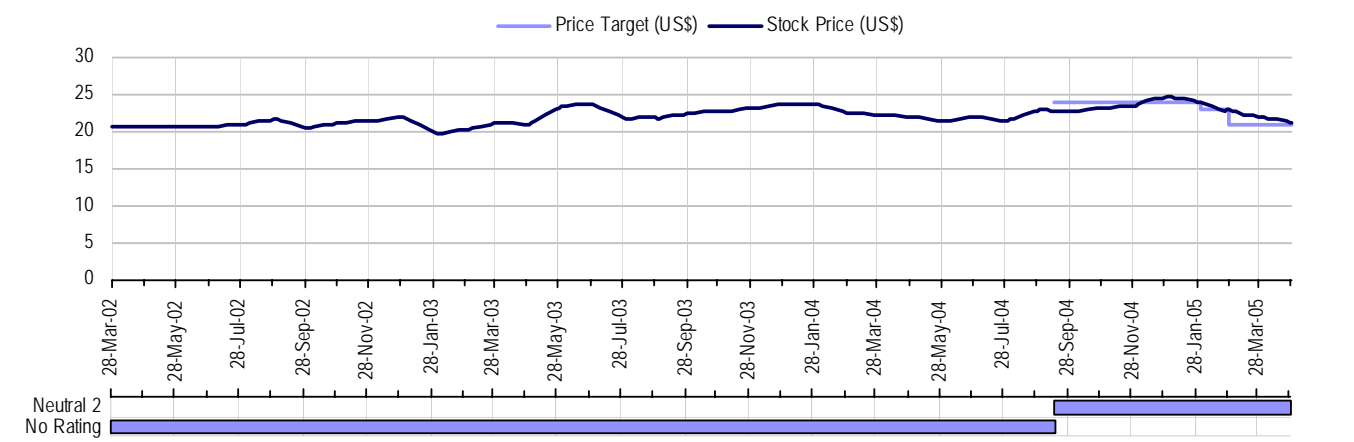
Company Name	Reuters	Rating	Price	Price date/time
Puget Energy Inc. <sup>4,5,6,16</sup>	PSD.N	Neutral 2	US\$21.20	28 Apr 2005 15:29 EDT

Source: UBS. EDT: Eastern daylight time.

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Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

Puget Energy Inc. (US\$)



Source: UBS; as of 28 April 2005.

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**PUGET ENERGY, INC.**

PSD – NYSE

May 3, 2005

**Rating:****NEUTRAL****Price:** (5/2/05) \$21.44**Price Targets:**

12-18 month: \$23

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

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FY (Dec)	2004A*	2005E**	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,198.9	\$2,414.7	10%	\$2,514.4	4%
Previous		\$2,566.7		\$2,515.5	
Price/Revenue ratio	1.0x	.9x		.9x	
<b>EPS Revised</b>	<b>\$0.55</b>	<b>\$1.44</b>	161%	<b>\$1.48</b>	3%
Previous		\$1.42		\$1.50	
Price/EPS ratio	38.9x	14.9x		14.5x	
<b>EBITDA (\$M)</b>	\$597.4	\$652.9	9%	\$698.6	7%
EV/EBITDA ratio	6.3x	5.8x		5.4x	

Quarterly Data:	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05A	<b>\$0.71</b>	\$0.62	\$741.7	\$801.5	\$215.9
6/30/05E	<b>\$0.15</b>	NC	\$456.8	\$547.1	\$123.8
9/30/05E	<b>\$0.04</b>	\$0.05	\$436.8	\$437.8	\$112.0
12/31/05E	<b>\$0.56</b>	\$0.60	\$779.4	\$780.4	\$201.2

\*See detail of footnotes on page 2.

**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (12/31/04)	50.5%
Cash per share (12/31/04)	\$0.21
Book value per share (12/31/04)	\$16.24
Dividend (yield)	\$1.00 (4.7%)
Return on Equity (T-T-M)	4%

**Trading Data**

Shares outstanding (M)	99.9
Market Capitalization (\$M)	\$2,141
52-week range	\$20.51 - \$24.81
Average daily volume (3 mos.) (K)	366
Float	99%
Index Membership	S&P 400 MidCap

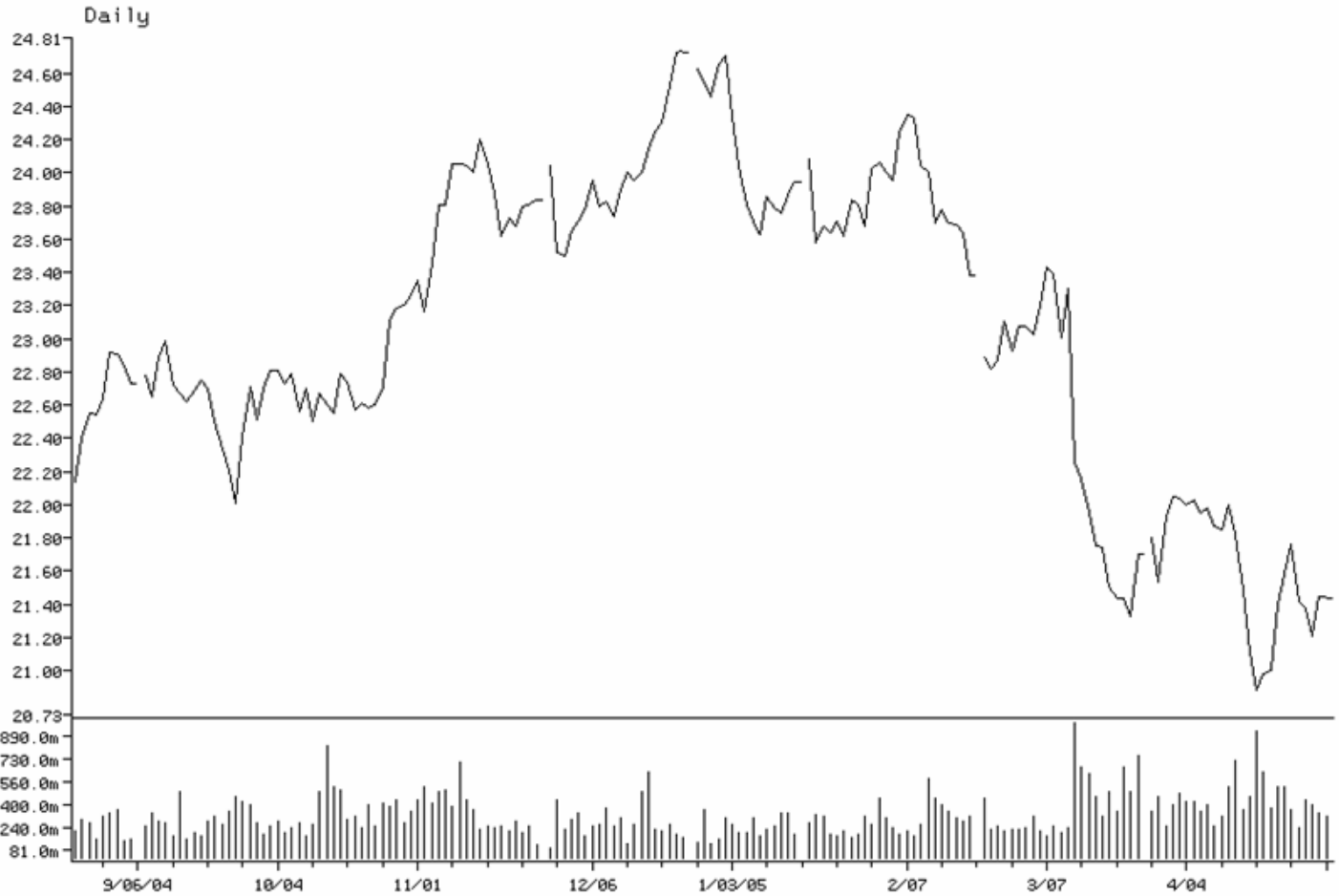
**Raising 2005 EPS Estimate as Quarterly Results Exceed Forecast. Maintaining Target Price and NEUTRAL Rating.**

- Puget Energy reported 1Q'05 diluted EPS of \$0.71, compared to \$0.67 for 1Q'04 and our forecast of \$0.62. The EPS result included a loss of \$0.01 at InfrastruX, which is now accounted for in discontinued operations. We were projecting income of \$0.01 from this utility services business that is being divested.
- The positive earnings variance from our forecast is primarily explained by the partial recovery of a previously reported regulatory disallowance (+\$0.04 per share) and lower storm related restoration costs (+\$0.03 per share) than we were expecting. Also helping quarterly results were the resolution of two rate cases in the past year (with an unidentified per share contribution), and lower interest expense (+\$0.02 per share).
- We are raising our 2005 EPS estimate of \$1.42 to \$1.44 to reflect the first quarter's positive earnings variance from our forecast, a reduction in our forecast from InfrastruX as a discontinued operation from \$0.04 to \$0.02, and other minor forecast changes. Our 2006 EPS forecast is modestly lowered from \$1.50 to \$1.48 due to lower estimates of other (non-regulated) revenues and lower other income.
- We are maintaining our 12-18 month target price of \$23, or 15.8x the average of our 2005 and 2006 EPS estimates. Over the past decade, the stock of PSD has traded at a median 12.8x multiple of year-forward earnings. With the share price below our target, we are maintaining our **NEUTRAL** rating.

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*Includes a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

\*\*Includes 1Q'05 benefit of \$0.04/sh. for partial recovery of a previously reported regulatory disallowance related to the Tenaska gas supply regulatory asset and on-going disallowance of approximately \$0.02.

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**Operating Results Higher Than Expectations**

Puget Energy reported 1Q'05 diluted EPS of \$0.71, compared to \$0.67 for 1Q'04. We were forecasting \$0.62.

The positive earnings variance from our forecast is primarily explained by the partial recovery of a previously reported regulatory disallowance (+\$0.04 per share) and lower storm related restoration costs (+\$0.03 per share) than we were expecting. Also helping quarterly results were the resolution of two rate cases in the past year (with an unidentified per share contribution), and lower interest expense (+\$0.02 per share).

Now viewed as discontinued operations, InfrastruX had a loss of \$0.01 per share. We were projecting income of \$0.01 per share. Since ownership in InfrastruX no longer fits its strategy, Puget is attempting to monetize its investment in this business through a sale or third party recapitalization. While it is uncertain how much InfrastruX may fetch, Puget says the sales proceeds will be invested in the regulated utility. Also, the timing of the InfrastruX divestiture is uncertain. Management has said it should be consummated before year-end 2005. Our earnings model continues to assume a mid-2005 divestiture.

**Earnings Benefits Greater than Earnings Drags**

Utility 1Q'05 EPS of \$0.72 compared to \$0.67 a year earlier, and our forecast of \$0.61. The aforementioned benefits to earnings were able to overcome the effects of milder temperatures (3% decline in heating degree days), a higher tax rate (39.0% vs. 36.9%), and an on-going Tenaska plant-related disallowance (-\$0.02 per share).

**Milder Temperatures Offset Customer Growth**

Quarterly electric revenues of \$420 million climbed \$28 million, or 7%. This increase was due primarily to a \$20 million improvement in retail sales and an \$8 million increase in wholesale, transportation, and other revenues. Retail sales rose because of the May 24, 2004 rate increase for the rate basing of the company's one-half interest in the Fredrickson plant and the March 4, 2005 general rate increase for electric and gas services. Retail volumes were up only 0.5%, as 2.0% customer growth was mostly offset by reduced usage because temperatures were 3% warmer than year ago.

After deducting the costs of generating and purchasing electric energy from electric revenues, Puget Sound Energy had electric margins of \$202 million during 4Q'04. These electric margins were up \$7 million, or 4%, primarily because the electric utility was not adversely impacted by excess power costs, as was the case a year earlier. Also helping the electric margin were the aforementioned electric rate increases and customer growth. These electric margin beneficiaries were partially offset by the \$3 million pretax regulatory disallowance in connection with gas supply costs for the Tenaska generating project.

Quarterly gas revenues of \$321 million rose \$45 million, or 16%, primarily due to higher tariffs under the current Purchased Gas Adjustment mechanism to recover higher purchased gas costs. Gas revenues also rose due to a 3.2% increase in customer growth, and an improved economy in the company's service territory in Washington, which was more than offset by slightly warmer temperatures and lower usage in response to higher natural gas prices. Heating-degree days from January 1, 2005 through March 31, 2005 in the company's service territory were 7% warmer than normal and 3% warmer than a year earlier. After deducting the costs of gas sales to retail and transportation customers from gas revenues, gas margins were \$88 million in 1Q'05, which were up \$0.5 million, or less than 1%, from 1Q'05.

**EPS Forecast Revisions**

Management reiterated 2005 EPS guidance of \$1.30-\$1.40, but did not say whether its 2006 EPS guidance of \$1.40-\$1.55 had changed.

We are raising our 2005 EPS estimate of \$1.42 to \$1.44 to reflect the first quarter's positive earnings variance from our forecast, a reduction in our forecast from InfrastruX as a discontinued operation from \$0.04 to \$0.02, and other minor forecast changes. The company continues to face a 2005 regulatory lag of recovering rising costs not reflected in the March 4, 2005 rate order (-\$0.15 per share) and on-going disallowances of certain Tenaska gas costs (-\$0.07 per share).

Our 2006 EPS forecast is lowered from \$1.50 to \$1.48 due to lower estimates of “other” (non-regulated) revenues and lower “other” income. Note: our 2006 projection of a 9% increase in consolidated net income is being diluted by a 6% increase in average shares outstanding, chiefly because of our assumption of a year-end 2005 offering of approximately 5.0 million shares to help finance capital expenditures, especially for two wind power projects.

Note we have re-combined results and forecasts from continuing operations into one segment. Previously, we separated earnings between regulated and non-regulated activities to more clearly keep tabs of the electric and gas business, having found over time that the timing of the utility’s non-regulated activities is not predictable. However, with the accounting of InfrastruX in discontinued operations, the company no longer breaks out non-regulated earnings from the company’s utility results.

**Maintaining Target Price and  
NEUTRAL Rating**

We are maintaining our 12-18 month target price of \$23, or 15.8x the average of our 2005 and 2006 EPS estimates. Over the past decade, the stock of PSD has traded at a median 12.8x multiple of year-forward earnings. With the share price below our target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.7%.

James L. Bellessa Jr., CFA  
Vice President, Senior Research Analyst  
406.791.7230



**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

**Assets****Utility Plant:**

	2000	2001	2002	2003	2004
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,389,882
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,881,768
Common plant	351,051	362,670	378,844	390,622	409,677
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,452,969)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,228,358

**Other Property and Investments:**

Investment in Bonneville Exchange Power Contract	58,189	54,663	51,136	47,609	
Goodwill, net	45,655	102,151	125,555	133,302	43,503
Intangibles, net		16,059	18,652	18,707	16,680
Non-utility property and equipment, net		48,369	80,855	91,932	
Other	188,453	96,007	101,932	110,543	257,785
Total other property and investments	292,297	317,249	378,130	402,093	317,968

**Current Assets:**

Cash	36,383	92,356	176,669	27,481	19,771
Restricted cash			18,871	2,537	1,633
Accounts receivable, net					
Less: Allowance for doubtful accounts					
Total accounts receivable	343,108	279,321	279,623	227,115	216,304
Unbilled revenues	211,784	147,008	112,115	131,798	140,391
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	107,356
Purchased gas receivable	96,050	37,228			19,088
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	8,087
Taxes receivable					
Prepayments and other	11,607	11,277	11,323	12,200	20,360
Total current assets	797,933	660,838	672,744	493,852	532,990

**Long-Term Assets:**

Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	127,252
PURPA buyout costs	243,071	244,635	243,584	227,753	211,241
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	13,765
Power cost adjustment mechanism				3,605	
Other	177,609	239,941	269,876	315,739	401,795
Total Long-term assets	628,030	680,909	690,388	698,513	754,053

<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,833,369</b>
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**Capitalization and Liabilities****Capitalization:**

Common stock	\$859,038	\$870	\$936	\$991	\$999
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,621,756
Earnings reinvested in the business	92,673	32,229	36,396	58,217	13,853
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(14,332)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,622,276
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,212,532
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,116,947

Minority interest in equity of a consolidated subsidiary

			10,629	11,689	4,648
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**Current Liabilities:**

Accounts payable	410,619	167,426	205,619	214,357	239,520
Short-term debt	378,316	348,577	47,295	13,893	8,297
Current maturities of long-term debt	19,000	119,523	73,206	246,829	38,933
Purchased gas liability	0	0	83,811	11,984	
Accrued expenses:					
Taxes	103,996	70,708	62,562	77,451	77,698
Salaries and wages	17,445	14,746	11,441	12,712	13,829
Interest	43,955	42,505	37,942	32,954	29,005
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	19,261
Tenaska disallowance reserve					3,156
Other	26,685	46,178	47,761	46,378	61,155
Total current liabilities	1,000,016	844,808	572,047	660,194	490,854
Deferred Income Taxes	608,185	605,315	730,675	755,235	810,726
Other Deferred Credits	132,869	196,339	267,458	340,893	409,945
Commitments and Contingencies	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	249
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,833,369</b>

## PUGET SOUND ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)

	2003	1Q04	2Q04	3Q04	4Q04**	2004**	1Q05	2Q05E	3Q05E	4Q05E	2005E	2006E
OPERATING REVENUES:												
Electric	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$ 1,423,034	\$420,090	\$322,279	\$338,896	\$442,955	\$1,524,220	\$1,587,317
Gas	634,230	275,692	119,479	89,432	284,703	769,306	321,129	134,065	97,397	335,908	888,499	925,071
Other	<u>6,043</u>	<u>527</u>	<u>553</u>	<u>2,925</u>	<u>2,531</u>	<u>6,537</u>	<u>434</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>1,934</u>	<u>2,000</u>
Total operating revenues	<u>2,041,016</u>	<u>668,714</u>	<u>423,123</u>	<u>415,026</u>	<u>692,012</u>	<u>2,198,877</u>	<u>741,653</u>	<u>456,844</u>	<u>436,793</u>	<u>779,363</u>	<u>2,414,653</u>	<u>2,514,387</u>
OPERATING EXPENSES:												
Energy costs:												
Purchased electricity	714,469	196,367	173,847	147,589	205,764	723,567	208,178	148,248	160,976	240,082	757,484	777,785
Purchased gas	327,132	162,407	63,703	44,574	180,618	451,302	201,744	73,244	51,263	214,885	541,136	558,722
Electric generation fuel	64,999	13,988	21,014	25,130	20,640	80,772	20,448	19,337	25,417	26,134	91,336	87,302
Residential Exchange	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(55,046)	(35,773)	(33,890)	(50,940)	(175,648)	(175,000)
Unrealized (gain)/loss on derivative instruments	106	(87)	(2,849)	1,894	516	(526)	509	0	0	0	509	0
Utility operations and maintenance	289,702	73,855	73,201	67,093	77,083	291,232	75,522	76,000	69,000	79,000	299,522	310,000
Other operations and maintenance	1,547	484	695	484	741	2,324	741	500	500	500	2,241	2,000
Depreciation and amortization	220,087	55,870	56,569	57,598	58,529	228,566	58,077	61,300	62,500	63,000	244,877	260,000
Merger and related costs/conservation amort.	33,458	8,190	4,809	4,747	4,942	22,688	5,162	5,000	5,000	5,000	20,162	24,000
Goodwill Impairment												
Taxes other than federal income taxes	194,857	64,224	42,354	42,756	59,575	208,990	69,700	47,000	47,000	64,000	227,700	233,000
Federal income taxes	<u>70,775</u>	<u>39,097</u>	<u>(5,433)</u>	<u>6,957</u>	<u>36,134</u>	<u>76,757</u>	<u>46,084</u>	<u>9,127</u>	<u>2,530</u>	<u>36,217</u>	<u>93,959</u>	<u>95,973</u>
Total operating expenses	1,743,292	559,972	392,548	364,808	593,868	1,911,199	631,119	403,983	390,297	677,878	2,103,277	2,173,782
OPERATING INCOME	297,724	108,742	30,575	50,218	98,144	287,678	110,534	52,861	46,496	101,485	311,376	340,605
OTHER INCOME	<u>1,587</u>	<u>68</u>	<u>1,570</u>	<u>356</u>	<u>2,392</u>	<u>4,362</u>	<u>1,164</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>2,664</u>	<u>2,000</u>
INCOME BEFORE INTEREST CHARGES	299,311	108,810	32,145	50,574	100,536	292,040	111,698	53,361	46,996	101,985	314,040	342,605
INTEREST CHARGES, net of AFUDC	178,488	42,043	41,842	41,104	41,574	166,539	39,582	41,250	42,750	45,250	168,832	184,000
Mandatorily redeemable securities interest	1,072	23	23	23	23	91	23	23	23	23	92	92
Preferred stock dividends of subsidiary	<u>5,151</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
INCOME FROM CONTINUING OPERATIONS	114,600	66,744	(9,720)	9,447	58,939	125,410	72,093	12,088	4,223	56,712	145,116	158,513
Discontinued Operations:	<u>1,766</u>	<u>(379)</u>	<u>2,940</u>	<u>1,677</u>	<u>(74,626)</u>	<u>(70,388)</u>	<u>(1,018)</u>	<u>3,000</u>	<u>0</u>	<u>0</u>	<u>1,982</u>	<u>0</u>
NET INCOME before effect of acct. change	116,366	66,365	(6,780)	11,124	(15,687)	55,022	71,075	15,088	4,223	56,712	145,116	158,513
FAS-133 transition adjustment loss (net of tax)	169					0						
INCOME FOR COMMON STOCK	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$71,075	\$15,088	\$4,223	\$56,712	\$145,116	\$158,513
DILUTED COMMON SHARES OUT. --WEIGHTED	95,309	99,367	99,371	100,043	99,765	99,911	100,446	100,746	101,046	101,346	100,896	107,296
INCOME FOR COMMON STOCK												
Utility	\$114,431	\$66,744	(\$9,720)	\$9,447	\$58,939	\$125,410	\$72,093	\$12,088	\$4,223	\$56,712	\$143,134	\$158,513
Discontinued Operations	1,766	(379)	\$2,940	\$1,677	(\$74,626)	(70,388)	(1,018)	\$3,000	\$0	\$0	1,982	0
Cumulative effect of accounting change	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$71,075	\$15,088	\$4,223	\$56,712	\$145,116	\$158,513
EARNINGS PER COMMON SHARE												
Utility	\$1.20	\$0.67	(\$0.10)	\$0.09	\$0.59	\$1.26	\$0.72	\$0.12	\$0.04	\$0.56	\$1.42	\$1.48
Discontinued Operations	\$0.02	(\$0.00)	\$0.03	\$0.02	(\$0.75)	(\$0.70)	(\$0.01)	\$0.03	\$0.00	\$0.00	\$0.02	\$0.00
Cumulative effect of accounting change	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>
DILUTED EARNINGS PER SHARE	\$1.22	\$0.67	(\$0.07)	\$0.11	(\$0.16)	\$0.55	\$0.71	\$0.15	\$0.04	\$0.56	\$1.44	\$1.48

\* We have attempted to conform our earnings model for the company's 1Q'05 decision to sell InfrastruX and to classify this utilities service business as a discontinued operation. While management has not yet provided restated data for 2Q'05, 3Q'05, 4Q'05, we have attempted to adjust our earnings model (even though not all rows and columns add), and use the assumption that InfrastruX will be divested by mid-2005, even though the company says it believes the transaction will be consummated by year-end 2005. \*\*Discontinued operations include 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

D.A. Davidson & Co.

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D.A. Davidson & Co. expects to receive, or intends to seek, compensation for investment banking services from this company in the next three months.

D.A. Davidson & Co. is a full service investment firm that provides both brokerage and investment banking services. James L. Bellessa, Jr., CFA, the research analyst principally responsible for the preparation of this report, will receive compensation that is based upon (among other factors) D.A. Davidson & Co.'s investment banking revenue. However, D.A. Davidson & Co.'s analysts are not directly compensated for involvement in specific investment banking transactions.

I, James L. Bellessa, Jr., CFA, attest that (i) all the views expressed in this research report accurately reflect my personal views about the common stock of the subject company, and (ii) no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

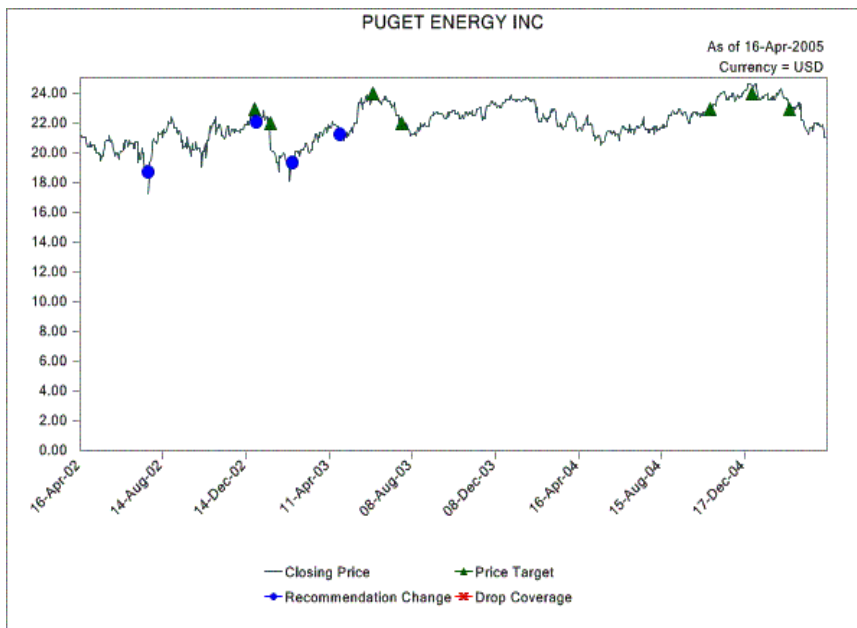
## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 3/31/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 40%	Neutral 50%	Underperform 10%
Corresponding Private Client Research Ratings and Distribution	Buy, Core/Buy 65%	Hold, Core/Hold 35%	Avoid 0%
Distribution of Combined Ratings	45%	47%	8%

### Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.

Institutional Coverage	8%	12%	7%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	6%	10%	7%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

### D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)

Buy, Neutral, Underperform

### D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)

Strong Buy, Buy, Neutral, Underperform

### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
22-Jul-2002	18.73	BUY	24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

**D.A. Davidson & Co.**

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

### **Other Disclosures**

Information contained herein has been obtained by sources we consider reliable, but is not guaranteed and we are not soliciting any action based upon it. Any opinions expressed are based on our interpretation of data available to us at the time of the original publication of the report. These opinions are subject to change at any time without notice. Investors must bear in mind that inherent in investments are the risks of fluctuating prices and the uncertainties of dividends, rates of return and yield. Investors should also remember that past performance is not necessarily an indicator of future performance and D.A. Davidson & Co. makes no guarantee, express or implied, as to future performance. Investors should note this report was prepared by D.A. Davidson & Co.'s Institutional Research Department for distribution to D.A. Davidson & Co.'s institutional investor clients and assumes a certain level of investment sophistication on the part of the recipient. Readers, who are not institutional investors or other market professionals, should seek the advice of their individual investment advisor for an explanation of this report's contents, and should always seek such advisor's advice before making any investment decisions. Further information and elaboration will be furnished upon request.

05.02.2005

**Puget Energy, Inc. (PSD)**

**Reports Q1 Earnings**

**\$21.51 | BUY**

- **Puget Energy is off to a solid start in 2005. Q1 operating earnings were \$0.67 per share, three cents ahead of the street estimate, and in line with results in the first quarter a year ago.**
- **Hopkins Ridge construction completion is due in December of this year. Wild Horse completion is due in December 2006.**
- **Earnings estimates remain unchanged at \$1.35 and \$1.48 for 2005 and 2006, respectively.**
- **PSD is rated Buy.**

52 Week High	\$24.81
52 Week Low	\$20.52
P/E	FY04A 13.9x
	FY05E 15.9x
	FY06E 14.5x
12 Mo. Price Target	\$26.00
Shares Out (Mil)	99.9
Market Cap (Mil)	\$2,148.6
Avg Daily Vol (000s)	355.7
Equity Ratio	40%
Book Value	\$16.24
Dividend	\$1.00
Yield	4.64%
3- 5 yr EPS Growth	3%
Fiscal Year End	Dec

**EPS ESTIMATES**

FY04A	\$1.55
FY05E	\$1.35
FY06E	\$1.48

▲ Puget Energy reported Q1 earnings of \$0.71 per share on a GAAP basis. Earnings from continuing operations were \$0.72 (excluding a \$0.01 loss associated with InfrastruX). Earnings included a \$0.04 one-time positive benefit associated with a favorable WUTC regulatory ruling (a reduction in the Tenaska disallowance). Operating earnings of \$0.67 still compared relatively favorably with the \$0.64 street estimate and the \$0.67 earned in the first quarter a year ago.

Heating degree days in the first quarter were 93 percent of normal, compared to 96 percent of normal in the first quarter a year ago. A reduction in storm-related outage expenses offset the impact of warmer winter weather.

The Hopkins Ridge wind power project continues to move forward with construction due to finish by December of this year. The Wild Horse wind power project should finish in December 2006. Capital expenditures in 2005 should be \$580 million, including \$280 million for energy delivery and \$200 million for Hopkins Ridge. Capital expenditures in the first quarter amounted to \$120 million.

While the next two quarters are likely to see normal seasonal weakness, the solid Q1 earnings figures gives us some additional level of comfort about our 2005 earnings estimates. Our 2005 earnings estimate remains unchanged at \$1.35 per share, as does our 2006 earnings estimate at \$1.48 per share. PSD is rated Buy.

**Additional required disclosures under NASD Rule 2711 are provided on the last page of this document.**

**Required Disclosures:**

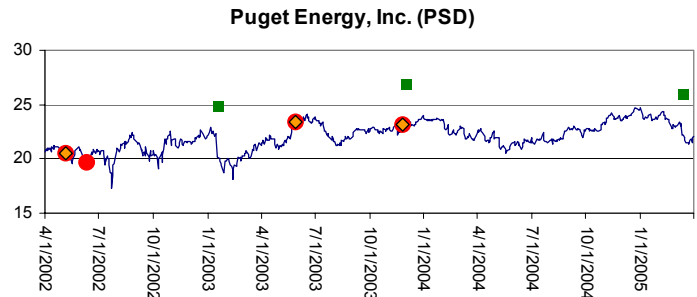
Paul C. Latta, CFA, [platta@mwrinc.com](mailto:platta@mwrinc.com), (206) 664-8897

- I, Paul C. Latta, hereby certify (1) that the views in this research note accurately reflect my personal views about any or all of the subject securities or issuers referred to in this note and (2) no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views in this note.

**Additional required disclosures under NASD Rule 2711 are provided on the last page of this report.**

As of March 31, 2005

	From	To	Date	Price
■	Price Target	\$27 to \$26	3/11/2005	\$22.25
■	Price Target	\$25 to \$27	12/1/2003	\$23.48
◆	Added to Focus List		11/26/2003	\$23.21
●	Hold to	Buy	11/26/2003	\$23.21
◆	Removed from Focus List		5/28/2003	\$23.40
●	Buy to	Hold	5/28/2003	\$23.40
■	Price Target	To \$25	1/16/2003	\$20.24
●	Rating System Change	Buy	6/11/2002	\$19.64
◆	Added to Focus List		5/6/2002	\$20.57
●	Hold to	Buy	5/6/2002	\$20.57



● Ratings Change ◆ Focus List Change ■ Target Price Change

Price targets are subject to change as new information becomes available, and reflect our current judgment regarding this security. Note that there are risks that may impede the achievement of a predicted price target. Price targets are based on fundamental factors such as historical and projected earnings, cash flow, discounted cash flow, relative book value, peer group evaluation, relative sector valuations, and expectations on general market and economic conditions.

McAdams Wright Ragen employs a Ratings System (in effect since 6/12/2002), defined as follows.

Buy/Addition to InStock Recommended List: We expect the Stock to Outperform the Market.

Hold/Addition to InStock Recommended List: We expect the Stock to be a Market Performer.

Sell/Removal from InStock Recommended List: We expect the Stock to Underperform the Market.

Ratings System in effect between 2/7/2002 and 6/12/2002: Strong Buy, Buy, Hold, Underperform, Sell.

Ratings System in effect prior to 2/7/2002: Buy, Moderate Buy, Hold, Underperform, Sell.

	Percentage of Rated Stocks Currently Assigned this Rating	Percentage of Rated Stocks with this Rating with which MWR has had an Investment Banking Relationship in the last 12 months
Buy	51%	9%
Hold	35%	4%
Sell	13%	0%

For Price Chart and Ratings History disclosures, please go to <http://www.mwrinc.com/ClientAccess/quotesresearch.html>, or to request information, please contact Sara E. Hasan, Research Assistant, (206) 664-8854, [mwr@mwrinc.com](mailto:mwr@mwrinc.com)

This is not a complete analysis of every material fact regarding any company, industry or security. The opinions expressed here reflect our judgment at this date and are subject to change. The information has been obtained from sources we consider reliable, but we cannot guarantee the accuracy. Our firm, or its officers, research personnel, other employees or customers may have long or short positions in the securities or options of the recommended issuers, may buy and sell the securities or options, may serve as an officer or director of any company mentioned, prior to or at the time of publication of the report or thereafter.

**Additional required disclosures under NASD Rule 2711 are provided on the last page of this document.**

# Puget Energy, Inc.

## Q1 Results – Beats Estimates; Lowering Price Target, Maintain Market Outperform

### Investment Summary

PSD reported first quarter results of \$0.71 compared to \$0.67 the prior year and above our \$0.60 estimate. The Utility division reported EPS of \$0.72 compared to \$0.67 the prior year. The InfrastruX division, which was classified as discontinued business, reported a loss of \$0.01 compared to a less than one cent loss the prior year. We are maintaining our FY'05 and FY'06 EPS estimates of \$1.36 and \$1.50, respectively. We are maintaining our Market Outperform rating and slightly tweaking our target price to \$24 from \$25.

- **Total revenues increased 10.9% to \$741.7 million mainly due to rate increases.** Electric margins increased by \$7.4 million mainly due to a favorable ruling in the Tenaska case for the PCA period II, which contributed \$6 million to the margin, or \$0.04 to the EPS. Gas margins were affected by warmer weather. Heating degree days were 7% lower than normal due to warmer weather and 4% lower than last year. Customer growth for the LTM ending March 2005 was 2% for electric and 3% for natural gas.
- **Operation and maintenance expenses increased 2.3% to \$75.5 million.** D&A increased approximately 4.0% to \$58.1 million due to infrastructure additions. Interest expense decreased 5.9% to \$39.6 million mainly due to lower interest debt.
- **InfrastruX reported a loss of \$0.01 compared to a loss of less than one cent the prior year.** The Company intends to sell this division by the end of fourth quarter this year making it a 100% regulated utility.
- **The Commission approved annual revenue increases of \$57.7 million and \$26.3 million on the electric and natural gas side,** respectively, which went into effect March 4, 2005.

### Valuation

We have used multiple approaches to value PSD's stock. Taking a weighted average of these approaches, we arrive at a \$24 target price, which represents roughly 12% upside at the current price level. Adding a dividend yield of 4.7%, there is a potential for total return of roughly 16%.

### Regional Growth May 4, 2005

**Puget Energy Inc**  
**PSD/NYSE**

**Closing Price on 5/3/05: \$21.49**  
**12-Month Price Target: \$24.00**  
**Previous 12-Month Price Target: \$25.00**  
**Market Outperform**

**Selman Akyol**  
**314-342-2158**  
**akyols@stifel.com**

**Vishal Sharma**  
**314-342-2164**  
**sharmav@stifel.com**

52-Week Range	\$20.51 – \$24.81
Average Daily Volume	363,454
Shares Outstanding	99.8 million
Market Capitalization	\$2,145 million
Market Cap./2005E Revenue	0.934x
Long Term Debt (Mil)	\$2,097
Total Debt / Total Capitalization	53%
Institutional Ownership	48%
Trailing 12 mo. Revenue	\$2,569 million
Book Value per Share (03/05)	\$16.50
Long-Term Projected EPS Growth	5%
Dividend	\$1.00
Dividend Yield	4.7%

#### Annual Estimates

FY (Dec)	2003A	2004A	2005E	2006E
Revs (Mil)	\$2,041	\$2,199	\$2,316	\$2,385
% chg y/y	2%	8%	5.3%	3%
<b>EPS</b>	<b>\$1.22</b>	<b>\$0.55*+</b>	<b>\$1.36</b>	<b>\$1.50</b>
Street	-	-	\$1.37	\$1.49
Price/EPS	17.6x	NMF	15.8x	14.3x

#### Quarterly EPS Estimates

FY (Dec)	Mar	Jun	Sep	Dec
2005E	\$0.71A	\$0.04	\$0.01	\$0.60
Street	-	\$0.14	\$0.07	\$0.57
2004A	\$0.67	(\$0.07)*	\$0.11	(\$0.16) <sup>+</sup>
2003A	\$0.45	\$0.22	\$0.10	\$0.45

\*Includes a \$0.28 charge related to Tenaska Order

<sup>+</sup>Includes a \$0.77 charge related to goodwill impairment

#### Required Disclosures: C-2

**See Page 5 for Required Disclosures**

**See Page 6 for Risks to Price Target**

#### Equity Research

1125 17th Street  
 Suite 1600  
 Denver, CO 80202  
 800-525-9899

**First Quarter Highlights**

PSD reported first quarter results of \$0.71 compared to \$0.67 the prior year. The increase in earnings was mainly due to an increase in electric margins. Electric margins increased \$7.4 million mainly as a result of a favorable ruling on the Tenaska, which contributed \$6 million to the margin, or \$0.04 to the EPS. Warmer weather adversely impacted gas volumes by 3.5%. Weather was 7% warmer than normal and 4% warmer than last year. This was partially offset by the rate increases implemented in March 2005. Customer growth continued to be above the national average at 2% on the electric side and 3% on the natural gas side. Operations and maintenance expenses increased 2.3% to \$75.5 million. D&A increased approximately 4.0% to \$59.1 million due to infrastructure additions. Taxes other than income taxes increased 8.5% to \$69.7 million due to higher revenues. Operating income increased 1.7% to \$110.5 million. Interest expense decreased 5.9% to \$39.6 million due to lower interest rate debt. InfrastruX reported a loss of approximately \$1 million, or \$0.01, compared to a loss of \$0.4 million, or less than a cent, the prior year. Net income increased 7.1% to \$71.1 million, and the shares outstanding remained essentially unchanged.

**InfrastruX**

The Company reported InfrastruX's results as discontinued operations in line with its intention to divest the business. The net investment in this division was \$34 million as net debt was \$160 million as of March 31, 2005. For the quarter, the division generated an EBITDA in the range of \$35 million. Assuming a 6-8 multiple would imply an equity value of \$50 to \$120 million. We would anticipate the Company reducing debt with the net proceeds pending any other uses.

**Balance Sheet**

Total Long-Term Debt at the end of December was \$2.1 billion or 53% of the total capital. The Company incurred approximately \$120 million in cap ex in Q1'05. PSD guided that its cap ex for 2005 will be approximately \$580 million, roughly \$200 million of which will be used on wind power projects.

**Outlook**

The Company highlighted that the Hopkins Ridge 160 MW Wind Project in Eastern Washington has been started and is expected to end in December this year. Another letter of agreement for the acquisition of Wild Horse Project in Kittitas County has been signed and is expected to clear regulatory processes by December 2006.

The Company has affirmed its earlier guidance of \$1.30-\$1.40 for FY 2005 and left its 2006 guidance of \$1.40-\$1.55 unchanged. The Commission approved \$57.7 million and \$26.3 million for electric and natural gas cases filed in 2004. These rates went into effect on March 4, 2004 and had minimal impact on the current quarter. The Company continues to increase its customer base above the national average. Customer growth for the LTM ended March 31, 2005 was 2% and 3% on electric and natural gas side. We view the divestment of the non-regulated portion of the business a positive, as it would make PSD a 100% regulated utility and aid the repayment of a portion of its debt from the sales proceed.

We are maintaining our FY'05 estimate of \$1.36, as the Company has maintained its guidance despite a good first quarter. The management noted that the utility earns roughly 80% of its earnings during the first and the fourth quarters. It has maintained a conservative approach as the third quarter is typically low, and will revisit the guidance when there is more visibility into the third quarter earnings. We have revised our estimates accordingly. We have also maintained our FY'06 EPS estimate of \$1.50, which is in line with the earlier guidance of \$1.40-\$1.55. This represents a 9.5% increase over 2005.

**Valuation**

We are slightly tweaking our target price to \$24 from \$25. We arrived at our new target price using multiple approaches (valuation sheet attached on page 3 of this report). We have basically valued PSD in line with the peer group. We calculated a weighted average of the prices arrived using multiple approaches to arrive at our target price. At this price there is a total return potential of roughly 16%, including a dividend yield of 4.7%. Hence, we rate this stock a Market Outperform.



**Valuation of PSD**

Expected Market Return (m)	10.0%
Risk Free Rate ( r)	4.2%
Beta (b)	0.76
Expected Return r+b(m-r)	8.6%

**Dividend Discount Model**

Annual dividend	\$1.00
Annual growth rate	5.0%
Estimated Price as per DDM	\$27.72

**Market Multiple**

	<u>Next FY</u>	<u>NTM</u>
Peer Group Multiples	15.9x	14.0x
PSD Multiples	15.9x	14.0x
EPS	\$1.36	\$1.50
Price at avg multiples	\$21.62	\$21.00

**Price to Book**

	<u>BV</u>
Peer Group Multiples	1.4x
PSD Multiples	1.4x
BV on 3/31/05	\$16.50
Price at avg multiples	\$23.10

**EV/EBITDA**

Peer Group Multiples	8.4x
PSD Multiples	8.4x
EBITDA - FY'05	\$620,608
EV at avg multiples	\$5,213,104
LT Debt-Cash	\$2,707,533
Equity	\$2,505,571
Diluted Shares	100,596
Price per share	\$24.91

**Weighted Average**

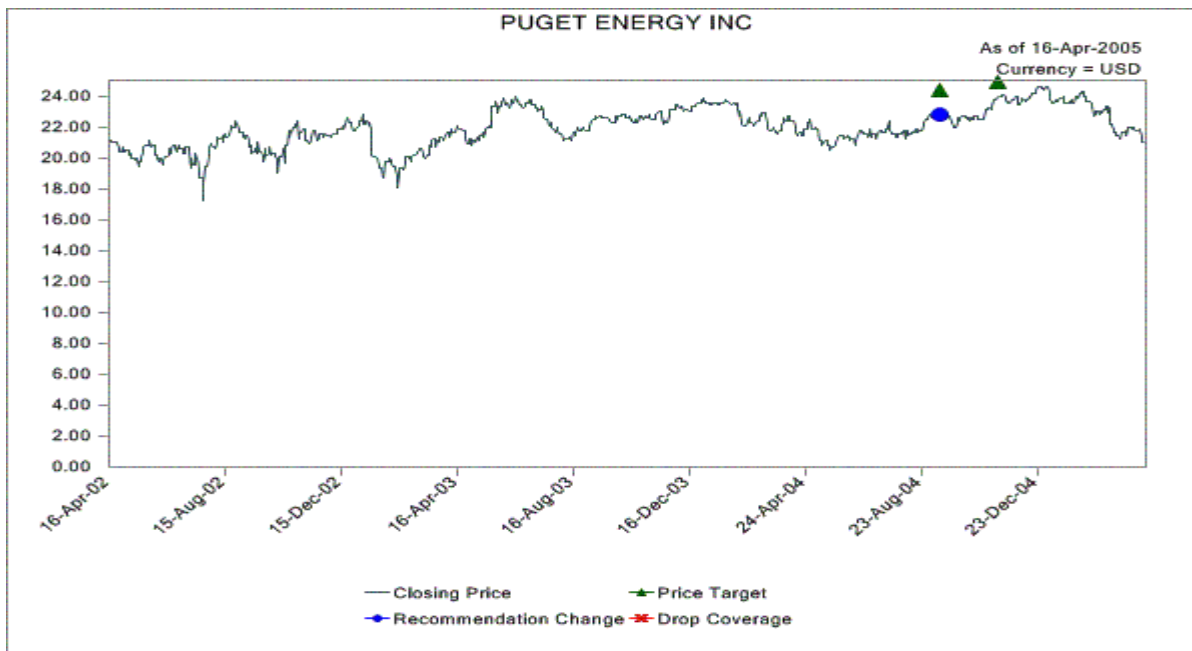
	<u>Price (p)</u>	<u>Weights (w)</u>	<u>p x w</u>
Dividend Discount Model	\$27.72	0.3	\$8.31
Market Multiple	\$21.31	0.3	\$6.39
P/B	\$23.10	0.2	\$4.62
EV/EBITDA	\$24.91	0.2	\$4.98
Weighted Average price			\$24.31
Rounded to			\$24.00
Closing price on 3/5/5			\$21.49
Estimated price appreciation			11.7%
Div Yield			4.7%
Estimated total return			16.3%



# Required Disclosures

Exhibit No. \_\_\_(BAV-5)

**EFFECTIVE NOVEMBER 13, 2002, STIFEL NICOLAUS ELIMINATED PRICE TARGETS ON PERFORM-RATED STOCKS. ALL MARKET OUTPERFORM AND MARKET UNDERPERFORM-RATED STOCKS CONTINUE TO HAVE PRICE TARGETS.**



## PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
09-Sep-2004	22.88	MARKET OUTPERFORM	08-Nov-2004	24.05	25.00
			09-Sep-2004	22.88	24.50

*We, the research analysts responsible for this report, attest that the views expressed in this research report accurately reflect our personal views about any and all of the subject securities or issuers. We have not received, and will not receive, compensation in return for the specific recommendations or views expressed by us in this report.*

**KEY FOR DISCLOSURES:** A – Stifel, Nicolaus makes a market in the common stock of this company. B – The analyst owns the common stock of this company. B-1 – A member of the analyst’s household owns the common stock of this company. C – Stifel, Nicolaus has managed or co-managed a public offering of securities for this company within the past 12 months. C-1 – Stifel, Nicolaus has been compensated for investment banking services by this company within the past 12 months. C-2 – Stifel, Nicolaus intends to seek compensation for investment banking services from this company in the next 3 months. D – The analyst serves on the Board of Directors of this company. D-1 – A member of the analyst’s household serves on the Board of Directors of this company. E – Stifel, Nicolaus beneficially owns in excess of 1% of a class of common equity securities of this company.

**RATING SYSTEM:** Market Outperform – The total return of the stock, adjusted for risk, is expected to outperform the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Perform – The total return of the stock is expected to perform in line with the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Underperform – The total return of the stock is expected to Underperform the broad U.S. equity market, defined as the Russell 2000, over the next 12 months. The security should be sold if such sale is consistent with clients' needs and objectives. Our 12-month price targets may temporarily vary from these expectations due to market volatility.

**RESEARCH COVERAGE:** As of March 31, 2005, Stifel Nicolaus had 213 companies under coverage. Stifel Nicolaus rated 104 companies, or 49%, as Market Outperform/“Buy,” 107 companies, or 50%, as Market Perform/“Hold,” and 2 companies, or 1%, at Market Underperform/“Sell.” During the previous 12 months, Stifel Nicolaus provided investment banking services for 23 of the companies rated Market Outperform/“Buy” (22%), 15 of the companies rated Market Perform/“Hold” (14%), and none of the companies rated Market Underperform/“Sell” (0%).

The information and statistical data contained herein have been obtained from sources we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to any changes in figures or our views.

**ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST.** Please contact the analyst for further information. Stifel, Nicolaus & Company, Inc. research is also available online at [www.multex.com](http://www.multex.com) and [www.firstcall.com](http://www.firstcall.com).

This is not a solicitation of any order to buy or sell.

**Risks to Price Target:**

**Specific risks to our price target include 1) an unanticipated unfavorable decision or less than estimated accretion from the pending rate case, 2) unanticipated unfavorable weather, and 3) unanticipated additional losses or charges relating to the divestiture of InfrastruX.**

**Price Target Valuation:**

Please refer to pages 2 and 3 of this report for a detailed discussion on the valuation method used in determining the Price Target.

# Investment Grade Research Company Update

July 22, 2005

Initiating Coverage

## Independent Power Producers & Utilities

### Puget Sound Energy, Inc.

[www.pse.com](http://www.pse.com)

NYSE: PSD

Selective Public Debt Issue as of July 22, 2005

Coupon %	Description	Maturity	Moody's/ S&P	Amount Outst. (\$mm)	Spread (bps)	Recommendation
5.483	Secured	6/1/35	Baa2/BBB	\$250	105	BUY

### Stable Credit Provides Good Value

We are launching coverage of Puget Sound Energy, Inc. (PSD) with a BUY recommendation on the secured debt of PSD subsidiary Puget Energy (PSE). The recommendation is supported by:

**Relative Value.** PSE's investment grade-rated first mortgage bonds (stable outlook) provide better value relative to similarly-rated names in the utility sector. We believe longer-term investors should benefit from (1) PSD management's conservative business strategy; and, (2) the stability of PSE's cash flows, which should result in minimal volatility in PSE's credit spreads.

**Strong Financials.** EBITDA coverage of interest has approximated 4.3x over the last twelve months ended March 31, 2005. We project EBITDA coverage of interest to rise to 4.6x during 2005. The balance sheet is adequate for investment grade, with a debt to capital of 53% at 1Q-05.

**Base rates set for two years.** PSE has no major base rate cases over the next 12 to 24 months. The most recent case concluded during 1Q-05, when the company was authorized an aggregate rate increase of roughly \$83 million for electric and gas service.

**Purchased power recovery.** PSE has the ability to recover the costs of most of its purchased power, which supplies about 70% of its energy requirements.

While expiring purchased power contracts and a growing need for power should result in expansion of power supply over the next several years, we believe that the Washington Commission prefers that PSE, the state's largest utility, remain strongly investment grade. For this reason, we do not expect future regulatory decisions to adversely impact PSE's credit ratings.

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Disclosures and Certifications can be found on the last page of this report.

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**Relative Value.** We compare PSE's 30-year first mortgage bonds to unsecured notes of Pacific Gas & Electric and AEP subsidiary Appalachian Power. Although there are differences in corporate strategies and operating characteristics between these companies and PSE, we believe these bonds are a good indication of where mid-BBB bonds trade. While PSE bonds trade modestly tighter than these comparisons, we like the PSE bonds for longer-term investors since: (1) PSE bonds are secured; (2) we view PSD management to have a more conservative strategy; and, (3) we believe there is greater predictability to Washington regulation than California over the longer term.

**Figure 1: Relative Trading Levels**

Company	Bond	Priority	Ratings	Spread (bps)
Puget Sound Energy (PSD)	5.483% due 6/1/35	Secured	Baa2/BBB	105
Appalachian Power (AEP)	5.95% due 5/15/33	Unsecured	Baa2/BBB	115
Pacific Gas & Electric (PCG)	6.05% due 3/1/34	Unsecured	Baa1/BBB	108

Source: Scotia Capital

**Company Description.** Puget Sound Energy (PSE), a subsidiary of Puget Energy, Inc. (PSD), is the largest electric and gas utility in the state of Washington. From 2002 through 2004, the utility generated approximately 85% of PSD's revenues and a higher portion (90%-100%) of cash flow. Although PSE is operated in a consolidated manner, we estimate that roughly 70-75% of PSE's cash flow is generated by the electric operations and 25-30% by the natural gas operations.

Following PSD's expected sale of InfrstruX during 2005, PSE is expected to be the sole cash flow provider to PSD. InfrastruX provides infrastructure-related construction and maintenance services to the electric and gas utility sectors throughout the U.S.

All of the bonds in the PSD structure are at the PSE level. However, some of these bonds were issued by different entities, reflecting the fact that PSE was formed by the 1997 merger between Puget Sound Power & Light and Washington Energy Co., whose primary subsidiary was Washington Natural Gas. See Figure 5 at the end of this report for a complete list of bonds.

## Washington Regulation Is A Significant Factor

In light of PSE's heavy reliance on purchased power and construction of new electric generating facilities to meet customer demand, the utility's financial condition is highly dependent upon constructive outcomes in the regulatory arena.

PSE is regulated by the three-member Washington Commission, which we view to be relatively neutral from an investor viewpoint. Equity return authorizations have tended to be slightly below the recent national average of 10.6%. Moreover, PSE has been unable to earn its authorized return in recent years due primarily to regulatory lag. We expect purchased power costs to be largely recoverable through 2006, but

prior Washington Commission decisions have denied recovery of modest expenditures related to a Tenaska contract. The company has the ability to recover energy conservation costs and receives a return on construction work in progress (CWIP).

Two of the three Commissioners have been appointed during 2005, lending some uncertainty as to the willingness of the Commission to continue a constructive dialogue with state utilities. However, we believe that regulatory decisions going forward should remain balanced, based upon PSE's ability to develop strong regulatory relationships, and the state's apparent intention to maintain the financial integrity of its utilities.

**General Rate Case.** In PSE's most recent general rate case concluded in February 2005, the Washington Commission authorized annual rate increases of \$56.6 million (4.5%) and \$26.3 million (3.5%) for PSE's **electric** and **gas** service, respectively. The rate increases were based upon an ROE of 10.3% and an overall return of 8.4%. PSE's total rate base of \$3.6 billion is comprised of \$2.5 billion in the electric division and \$1.1 billion in the gas division.

The company had filed for required rate increases of \$99.8 million and \$49 million for electric and gas service, respectively. PSE had sought an 11.75% ROE on a 75% common equity to capital ratio. A significant difference between the company's position and the final Commission determination was the lower return adopted by the Commission, versus the 11.75% ROE requested by PSE.

**Recovery of Purchased Power Costs.** PSE purchases roughly 70% of its power for customers from various third parties. Costs are recovered through a Purchased Cost Adjustment (PCA). PSE's exposure to purchased power costs over a four-year period ending June 30, 2006 is limited to \$40 million plus 1% of the excess. To date, the company has incurred costs up to the \$40 million cap, thereby limiting potential exposure to under-recovery of purchased power costs to 1% of the excess through June of next year.

On June 7, PSE filed for approval to recover higher purchased power costs driven by higher natural gas prices, and to recover the cost of the Hopkins Ridge Wind Project. The proposed rate increase of 3.65% would become effective December 1.

**Prior Power Cost Only Rate Cases (PCORCs).** The most recent PCORC concluded during May 2004, when the company was authorized recovery of \$44 million, in part to recover costs associated with Frederickson I electric generation facility.

Guidelines for establishing recovery of the Tenaska contract were also established. PSE's Tenaska contract, which expires in 2011, enables the utility to purchase 216 average MW of energy and 245 MW of capacity. PSE supplies the natural gas for the cogeneration facility. While the Commission disallowed recovery of \$43.4 million for prior years, partial recovery through the 2011 term of the Tenaska contract appears to be relatively certain. PSE would not be expected to fully recover the costs if the index price of natural gas exceeds the cost of natural gas embedded in the contract. In

light of current natural gas prices, we estimate that PSE may modestly under-recover costs associated Tenaska over the next several quarters.

Effective July 1, 2006, PSE is expected to share the differences in annual purchased power costs (from predetermined baseline costs) for each 12-month period starting in July in the following manner.

**Figure 2: Purchased Power Sharing Program**

Annual Pwr Cost Variability	Customers' Share	Company's Share
+/- \$20 million	0%	100%
+/- \$20 - \$40 million	50%	50%
+/- \$40 - \$120 million	90%	10%
+/- \$120 million	95%	5%

Source: Company Reports

As a result, if purchased power costs are \$120 million higher than expected, PSE would absorb \$38 million. Conversely, if costs are \$120 million lower than expected, PSE would receive a \$38 million benefit. PSE is required to submit a filing by Feb. 28, 2006 to reset the PCA power cost baseline rates that would become effective next year.

## Power Supply Is Mainly Purchased

PSE, a winter peaking utility, has historically purchased a significant portion of power supply from third parties. We expect this trend to continue.

**Figure 3: Puget 2004 Power Supply**

	MW	MWHR	% of Requirements
<b>RESOURCES</b>			
Hydroelectric	234	1,130,180	5.0%
Coal	677	5,119,002	22.6%
Nat gas/oil	902	799,088	3.5%
<b>Controlled resources</b>	1,813	7,048,270	31.1%
Other Sources			
Columbia River PUD contracts	1,350	5,231,691	23.1%
Other Hydroelectric	177	600,557	2.7%
Other Producers	1,011	3,589,298	15.9%
Short term purchases	---	6,164,457	27.2%
<b>Total Resources</b>	4,351	22,634,273	100.0%
<b>SALES (Mwhrs)</b>			
Retail		19,884,193	93.8%
Wholesale		1,317,394	6.2%
<b>Total Sales</b>		21,201,587	100.0%

Source: Company Reports



While significant dependence on hydroelectric resources, at a time when water levels are below normal, has tended to increase purchased power costs as PSE has had to rely upon purchases from natural-gas fired electric facilities, purchased power costs are largely recoverable from ratepayers. A summary of specific purchased power contracts follows.

**Columbia River Projects.** During 2004, 23.1% of the company's energy output was obtained at an average cost of approximately \$0.0146 per kWh through long-term contracts with several Washington Public Utility Districts (PUDs) which own hydroelectric projects on the Columbia River.

Under these contracts, PSE's payment includes a proportionate share of the annual cost of each project, including debt service costs, regardless of whether or not the projects operate.

**Figure 4: Puget Columbia River Contracts**

	Contract Expiration (Year)	Total Bonds Outstanding (as of YE-04) (\$ millions)	% of Output	Capacity (MW)	Cost (\$ millions)
Rock island					
Original Units	2012	\$ 115.8	50.0%	414	\$ 40.8
Additional Units	2012	\$ 328.4	75.0%		
Rocky Reach	2011	\$ 383.0	38.9%	505	\$ 24.7
Wells	2018	\$ 143.3	31.3%	261	\$ 5.2
Priest Rapids	2005	\$ 179.7	8.0%	72	\$ 2.4
Wanapum	2009	\$ 181.6	10.8%	98	\$ 3.3
<b>Total</b>		<b>\$ 1,331.8</b>		<b>1,350</b>	<b>\$ 76.4</b>

Source: Company Reports

**Other Significant Contracts Include:**

**Northwestern Corp. Contract.** NorthWestern provides PSE 71 MW of energy (97 MW of peak capacity) over a 21-year period, through December 2010.

**Pacific Gas & Electric (PG&E) Contract.** PSE has an ongoing exchange agreement with PG&E under which 300 MW of capacity and up to 413,000 MWh of energy are exchanged seasonally each year. No payments are made under this agreement, and contract may be terminated by either utility after giving five years' notice.

**Powerex Contract.** PSE has a power exchange agreement with Canadian utility Powerex which expires during 2006. Under this arrangement, Powerex pays PSE for the right to deliver up to 1,200,000 MWh annually to PSE at the Canadian border in exchange for PSE delivering power to Powerex.

**Sumas Cogeneration Contract.** PSE executed a 20-year contract to purchase 108 average MW of energy and 123 MW of capacity, beginning in April 1993, from Sumas,

which owns and operates a natural gas-fired cogeneration project located in Washington.

**March Point Cogeneration Contracts.** PSE has two contracts with March Point, which operates a natural gas fired cogeneration facility in Anacortes, WA. Both contracts, which provide as much as 140 MW of aggregate capacity, terminate during 2011.

#### **New Generation Facilities Expected.**

**Hopkins Ridge.** On March 11, 2005, PSE completed the acquisition of this wind project from Blue Sky Wind, LLC in southeastern Washington State. The maximum total capacity of the project is expected to be 150 MW, when completed by YE-05.

**Wild Horse.** In September 2004, PSE agreed to buy the proposed Wild Horse wind project in central Washington, which is slated to come on line during 2006. Total capacity of the project is expected to be 150 MW to 230 MW, at a cost of \$300 million to \$350 million, when completed in 2006.

#### **Natural Gas Operations Provide Steady Returns.**

PSE recovers natural gas costs through a purchased gas adjustment (PGA) clause. Effective October 1, 2004, a PGA increase raised rates by 17.6% annually. PSE's gas margin and net income are not affected by PGA modifications.

PSE enters into contracts for all of its natural gas supply from a variety of suppliers in the U.S. and Canada. During the 2004-2005 winter heating season PSE expected to receive:

- 22.7% of peak requirements from sources in British Columbia, Canada;
- 5.7% of peak supplies from Alberta, Canada;
- 16.6% of peak requirements from U.S. suppliers; and,
- The balance of the peak-day requirements from the Jackson Prairie and Clay Basin storage facilities; LNG; and, other sources. PSE owns one-third of the Jackson Prairie facility.

All of the utility's gas supply flows to PSE's service territory through Williams' subsidiary Northwest Pipeline Corp. (NWP), the sole interstate pipeline which serves the western Washington area. Contracts expire at various times over the next twelve years. PSE also has firm transportation capacity contracts with pipeline companies that deliver natural gas to NWP, including Duke Energy subsidiary Westcoast Energy, and TransCanada's Alberta and British Columbia systems.

Following problems on two of NWP's pipelines, the pipeline filed a request for authorization from the FERC to replace all of the lost capacity through construction of new facilities. NWP expects to complete the project by YE-06, which could increase PSE's costs by approximately 20% beginning in 2007. Importantly, PSE expects that

the increase would be entirely recoverable from customers through the PGA mechanism.

## Financial Outlook

We project steady growth at PSE, based upon the positive impacts from the 2005 rate case decision, investments in new energy resources, and continued expectations for recovery of purchased power costs. We expect EBITDA to approximate \$752 million during 2005, up from \$743 million during 2004. We assume electric and natural gas distribution volumes grow by roughly 2% year-over-year.

**Capital Expenditures.** PSE anticipates robust capital expenditures during 2005-06, reflecting the purchase of new wind generation facilities (roughly \$500 million over the two-year period) and upgrades to the natural gas and electric distribution systems. The capital budget should approximate \$600 million and \$700 million during 2005 and 2006, respectively, with roughly \$400 million related to improving the electric and gas distribution systems. We anticipate both debt and common stock to be issued as the company incorporates new generating projects into the system. Another source of cash would be generated by the sale of InfrastruX. PSD owns 91% of this asset, which was written down to a book value of \$33.4 million during 2004. We expect proceeds to approximate book value.

**Balance Sheet.** PSE's balance sheet reflects investment grade ratings. Debt to capital was about 53% at 1Q-05, virtually unchanged versus 1Q-04. (See summary at end of this report.) We do not expect significant modifications to the ratio over the next two years, based upon our assumption that both common stock and debt would be issued to fund any shortfalls in the capital budget.

We anticipate debt issuance to be secured. As of March 31, 2005, PSE had the ability to issue \$281 million of first mortgage bonds under the electric indenture, \$192 million of first mortgage bonds under the gas indenture, \$510 million of preferred stock at an assumed rate of 6.75%, and \$185 million of unsecured long term debt. The first mortgage bond issuance limitation given by PSE assumes the company maintains interest coverage of 2.0x and 1.75x, for the electric and gas division, respectively.

In March 2005, PSE amended its unsecured credit line agreement to increase total borrowing capacity to \$500 million, from \$350 million, and to extend the maturity to April 2010. Another source of liquidity is a \$150 million receivables securitization program which expires in December 2005. At 1Q-05, there was \$97.1 million in commercial paper outstanding and \$0.5 million outstanding under a letter of credit, effectively reducing the available borrowing capacity under these liquidity facilities to \$552.4 million. Parent PSD has a \$5.0 million credit line, which was reduced from a prior level of \$20 million.

Figure 5: Puget Energy, Inc. Fixed Income Securities

<b>Puget Energy, Inc.</b>		
\$5 mill line of credit		
<b>Puget Sound Energy, Inc.</b>	Short Term:	\$500 mill unsecured credit line due 4/2/10 \$150 mill receivables program due Dec 05
<b>Total Long Term Debt:</b>	<b>\$ 2,383.1</b>	
<b><u>Bonds Issued By Puget Power &amp; Light &amp; PSE</u></b>		
8.06% due 6/19/06	\$ 46.0	<b><u>Bonds Issued By Washington Gas</u></b>
8.14% due 11/30/06	\$ 25.0	6.92% due 9/12/05
7.75% due 2/1/07	\$ 100.0	6.92% due 9/12/05
7.61% due 9/8/08	\$ 25.0	6.93% due 9/13/05
3.363% due 6/1/08	\$ 150.0	6.58% due 12/21/06
6.46% due 3/9/09	\$ 150.0	7.02% due 9/11/07
7.96% due 2/22/10	\$ 225.0	7.04% due 9/12/07
7.69% due 2/1/11	\$ 260.0	6.53% due 8/18/08
6.74% due 6/15/18	\$ 200.0	6.51% due 8/19/08
7.00% due 3/8/29	\$ 100.0	6.61% due 12/21/09
PCBs due 2031	\$ 161.9	6.62% due 12/22/09
5.483% due 6/1/35	\$ 250.0	7.12% due 9/13/10
7.02% due 12/1/27	\$ 300.0	6.83% due 8/19/13
<b>Total PSE Bonds</b>	<b>\$ 1,992.9</b>	6.90% due 10/1/13
8.231% due 6/1/27	\$ 37.8	7.35% due 9/11/15
8.40% due 6/30/41	\$ 200.0	7.36% due 9/15/15
<b>Bonds Plus Preferred</b>	<b>\$ 2,230.6</b>	9.57% due 9/1/20
		7.15% due 12/19/25
		7.20% due 12/22/25
		<b>Subtotal</b>
		<b>\$ 152.5</b>

Source: Company Reports; Bloomberg

Figure 6: PSD Summary Historical & Projected Financials

HISTORICAL FINANCIAL INFORMATION										PROJECTIONS			
	1Q 04	2Q 04	3Q 04	4Q 04	1Q 05	YR 04	LTM	2Q 05	YR 05	YR 06			
<b>Consolidated Financials</b>													
<i>Profitability/Cash Flow</i>													
<b>EBITDA</b>	\$ 216.8	\$ 95.4	\$ 131.2	\$ 299.8	\$ 220.4	\$ 743.1	\$ 746.7	\$ 136.6	\$ 751.9	\$ 794.9			
Interest Expense	\$(43.4)	\$(43.3)	\$(42.9)	\$(43.5)	\$(41.1)	\$(173.1)	\$(170.7)	\$(42.3)	\$(162.0)	\$(168.0)			
Income Taxes	\$(38.7)	\$ 2.9	\$(8.5)	\$(30.7)	\$(46.1)	\$(75.0)	\$(82.3)	\$(24.0)	\$(74.0)	\$(79.0)			
Capital Expenditures	\$(75.9)	\$(167.6)	\$(94.1)	\$(96.7)	\$(124.4)	\$(434.3)	\$(482.7)	\$(150.0)	\$(600.0)	\$(700.0)			
Common Dividends	\$(21.6)	\$(22.0)	\$(21.4)	\$(21.8)	\$(21.9)	\$(86.9)	\$(87.2)	\$(22.0)	\$(88.0)	\$(92.0)			
<b>EBITDA less Op Costs &amp; Divs.</b>	\$ 37.1	\$ (134.6)	\$ (35.7)	\$ 107.2	\$ (13.0)	\$ (26.1)	\$ (76.2)	\$ (101.7)	\$ (172.1)	\$ (244.1)			
<i>Credit Stats</i>													
EBITDA/Interest	4.99x	2.20x	3.06x	6.90x	5.37x	4.29x	4.37x	3.23x	4.64x	4.73x			
Debt/EBITDA	---	---	---	---	---	3.04x	2.94x						
Total Debt	\$ 2,207.3	\$ 2,217.7	\$ 2,332.9	\$ 2,259.8	\$ 2,197.4	\$ 2,259.8	\$ 2,197.4						
Total Preferred + TOPrs	\$ 282.1	\$ 282.1	\$ 282.1	\$ 282.1	\$ 282.1	\$ 282.1	\$ 282.1						
Total Common Equity	\$ 1,701.6	\$ 1,679.2	\$ 1,661.3	\$ 1,622.3	\$ 1,680.8	\$ 1,622.3	\$ 1,680.8						
Total Capital	\$ 4,191.0	\$ 4,179.0	\$ 4,276.3	\$ 4,164.2	\$ 4,160.3	\$ 4,164.2	\$ 4,160.3						
Debt/Capital	52.7%	53.1%	54.6%	54.3%	52.8%	54.3%	52.8%						
<b>OPERATING STATISTICS</b>													
	1Q 04	2Q 04	3Q 04	4Q 04	1Q 05	YR 04	LTM	2Q 05	YR 05	YR 06			
<b>Electric Sales Statistics (mWhrs)</b>													
Total Retail Sales	5,601,996	4,357,889	4,462,421	5,461,887	5,630,327	19,884,193	19,912,524	4,418,268	20,083,035	20,283,865			
Total Wholesale Sales	269,610	281,680	379,280	386,824	345,784	1,317,394	1,393,568	295,623	1,343,742	1,357,179			
Total Energy Sales	5,871,606	4,639,569	4,841,701	5,848,711	5,976,111	21,201,587	21,306,092	4,713,891	21,426,777	21,641,045			
Transportation	483,702	459,713	530,204	515,346	522,026	1,988,965	2,027,289	503,208	2,287,310	2,310,183			
Energy Sales & Transportation	6,355,308	5,099,282	5,371,905	6,364,057	6,498,137	23,190,552	23,333,381	5,217,099	23,714,087	23,951,227			
<b>Natural Gas Operating Statistics ('000 therms)</b>													
Natural gas sales to customers	318,338	126,004	87,676	276,540	308,203	808,558	798,423						
Transportation volumes	56,182	47,415	45,238	52,808	53,126	201,642	198,587						
Total gas volumes	374,520	173,419	132,914	329,348	361,329	1,010,200	997,010						

Source: Company Reports; Scotia Capital Projections

## Scotia Capital (USA) Inc. (“SC-USA”)

Buy recommendation 19.3%  
Hold/Neutral recommendation 77.7%  
Sell recommendation 3%  
as of quarter ending June 30, 2005

### *Definition of Recommendations:*

**Buy:** The bond is projected to outperform the investment grade corporate bond market over the next 12 months.

**Hold:** The bond is projected to perform approximately in line with the investment grade corporate bond market over the next 12 month.

**Sell:** The bond is projected to underperform the investment grade corporate bond market over the next 12 months.

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- (i) the views expressed in this research report accurately reflect his or her personal views, and
- (ii) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

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August 1, 2005

**PUGET ENERGY, INC.**  
PSD – NYSE**Rating:****NEUTRAL****Price:** (7/29/05) \$23.38**Price Targets:**

12-18 month: \$23

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

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**Second Quarter 2005 Earnings Preview.**

- Puget Energy is scheduled to report earnings for its second quarter, ended June 30, 2005, on Tuesday August 2<sup>nd</sup>, after the market closes. A conference call with management will be held on Wednesday, August 3<sup>rd</sup> at 10:00AM EDT/7:00 AM PDT.
- We are looking for EPS of \$0.15 versus a loss of \$0.07 per share last year. Normalized earnings for 2Q'04 were \$0.18. Earnings in 2Q'04 included an after-tax charge of \$0.25 per share for a regulatory disallowance of certain gas costs of the Tenaska generating plant. The consensus estimate for 2Q'05 is \$0.12 per share.
- Results were unlikely helped by the weather. Heating degree days for the 2Q'05 "shoulder months" in PSD's service territory were 13% below normal, but were 11% above last year's totals. Also, temperatures primarily in June in the Pacific Northwest have been much milder than other parts of the United States, which is evident by the company's total cooling degree days, which were 86% and 56% of normal and last year's levels, respectively.
- Results could be aided by the 4.1% increase in electric rates that was approved by state regulators in March of 2005, while being held back by increased fuel costs, which caused the company to request a small rate increase in electric rates in July 2005, and other regulatory lags.

**RESEARCH NOTE**

D.A. Davidson & Co.

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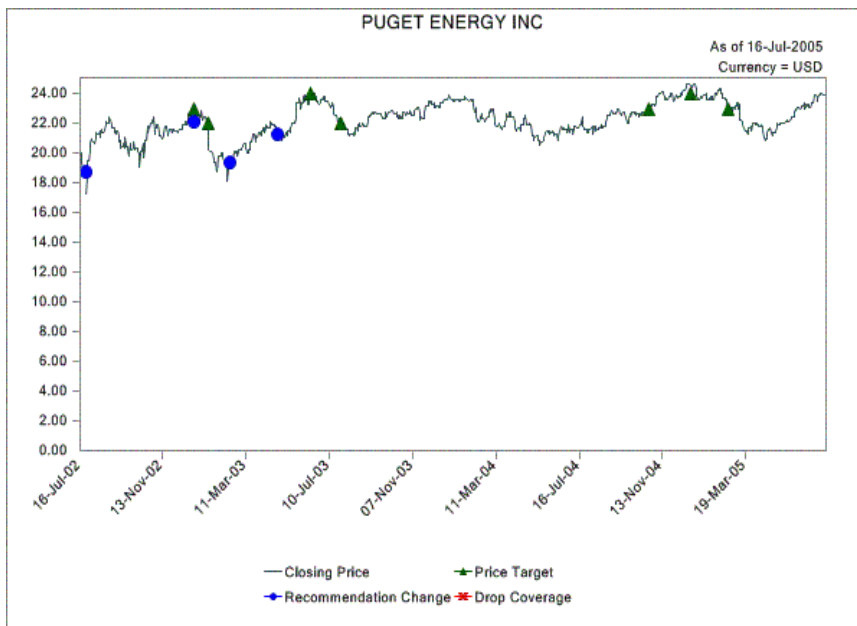
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## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 6/30/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 42%	Neutral 51%	Underperform 7%
Corresponding Private Client Research Ratings and Distribution	Buy, Core/Buy 76%	Hold, Core/Hold 24%	Avoid 0%
Distribution of Combined Ratings	48%	47%	6%

Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.			
Institutional Coverage	9%	10%	9%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	7%	9%	9%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

### D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)

Buy, Neutral, Underperform

### D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)

Strong Buy, Buy, Neutral, Underperform

#### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
22-Jul-2002	18.73	BUY	24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

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# UBS Investment Research

## Puget Energy Inc.

Americas	
Electric Utilities	
<b>Rating</b>	<b>Neutral 2</b> <i>Unchanged</i>
<b>Price target</b>	US\$23.00 <i>Unchanged</i>
<b>Price</b>	US\$23.50

### In-Line Results

■ **2Q05 in-line with expectations**

Puget realized recurring 2Q05 EPS of \$0.15, comparable to levels achieved in 2Q04. These numbers were in line with our estimate and \$0.04 above the Street consensus of \$0.11. Note that we adjust the reported EPS of \$0.12 for a one-time true-up of previously reported gas costs (\$0.03). Earnings for the quarter were driven by increased margins at the utility, offset by higher O&M and D&A.

■ **Maintaining 2005 and 2006 estimates**

We are maintaining our recurring 2005 and 2006 EPS estimates at \$1.40 and \$1.50, respectively.

■ **Regulatory overhang continues**

No material developments have been disclosed to ease us into our comfort zone regarding the several regulatory issues facing the company. However, we acknowledge the strides Puget has taken to reduce leverage to 60% at the end of 2004 from 70% in 2003 and the progress on its Least Cost Plan (LCP) with the addition of two wind projects.

■ **Valuation: Maintaining Price Target at \$23**

Our PT is derived using DCF analysis and implies a 15.3x PE on our recurring 2006 EPS.

RIC: PSD.N BBG: PSD US  
**3 August 2005**

**Trading data**

52-wk. range	US\$24.73-20.88
Market cap.	US\$2.35bn
Shares o/s	99.9m
Free float	80%
Avg. daily volume ('000)	250
Avg. daily value (US\$m)	5.7

**Balance sheet data 12/05E**

Shareholders' equity	US\$1.78bn
P/BV (UBS)	1.1x
Net cash (debt)	(US\$2.51bn)

**Forecast returns**

Forecast price appreciation	-2.1%
Forecast dividend yield	4.3%
Forecast stock return	+2.2%
Market return assumption	9.1%
Forecast excess return	-6.9%

**EPS (UBS, US\$)**

	12/05E		12/04 Actual
	From	To	
Q1	0.65	0.68	0.72
Q2	0.15	0.15	0.12
Q3E	0.07	0.07	0.04
Q4E	0.55	0.52	0.55
12/05E	1.40	1.40	1.38
12/06E	1.50	1.50	1.50

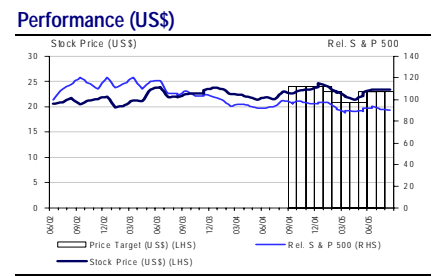
Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,188	2,386	-
EBIT	377	418	396	435	-
Net income (UBS)	110	155	146	167	-
EPS (UBS, US\$)	1.16	1.55	1.40	1.50	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	18.1	18.2	-
ROIC (EBIT) %	-	9.3	8.5	8.9	-
EV/EBITDA x	-	6.9	7.1	6.8	-
PE (UBS) x	-	14.6	16.8	15.7	-
Dividend yield %	-	4.4	4.3	4.3	-

Source: Company accounts, Thomson Financial, UBS estimates. UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.  
 Valuations: based on an average share price that year, (E): based on a share price of US\$23.50 on 03 Aug 2005 12:56 EDT

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**ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 5**

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## Earnings Summary

Puget realized a recurring 2Q05 EPS of \$0.15, comparable to levels achieved in 2Q04. These numbers were in line with our estimate and \$0.04 above the Street consensus of \$0.11. Please note, we adjust the reported EPS of \$0.12 for a one-time true-up of previously reported gas costs (\$0.03 per share). We also clean the reported 2Q04 EPS by \$0.25 of regulatory disallowance related to Tenaska. Earnings for the quarter were driven by an increase in the electric margin and an increase in gas margin before the gas true-up charge. Offsets were led by higher O&M followed by higher depreciation and amortization and other.

Management reiterated recurring EPS guidance at \$1.30 –1.40 for 2005 and \$1.40 – 1.55 for 2006, respectively. Puget expects its 2005 earnings to be minimally impacted by power costs falling outside the baseline as it reached its power cost adjustment (PCA) capacity last year. Further, customers will absorb 99% of the increase in variable power cost until mid-2006.

**Wind Update:** Management provided an update with respect to the two recently announced wind power projects – the 150 MW Hopkins Ridge project and the 160 MW Wild Horse project. Construction of the Hopkins Ridge project began in 1Q05 and the plant is on plan to be operational by December 2005. The Wild Horse project is currently moving through a permitting process and is expected to be completed by the end of 2006.

## Our View

While the second quarter results were in-line with our estimates, we are still cautious given the regulatory uncertainty around the company. The three large issues continue to include recovery of the earnings lag on the delivery capex, recovery of the two proposed wind additions and treatment of the Power Cost Adjustment (PCA) Mechanism post July 2006. No material developments have been disclosed to ease us into our comfort zone; however, we acknowledge the strides the company has taken to right size its balance sheet including leverage reduction to 60% at the end of 2004 from 70% in 2003. Major immediate catalysts for this stock would be positive rate recovery ruling on its soon to be completed Hopkins Ridge wind farm in 2005 and the future of the PCA mechanism.

## Maintaining Estimates

We are maintaining our recurring 2005 EPS estimate at \$1.40, which compares with the First Call consensus estimate of \$1.38 (reflecting a range of \$1.36 – 1.44). We are also maintaining our 2006 EPS estimate at \$1.50. This compares with the Street consensus estimate of \$1.50 (reflecting a range of \$1.45 – 1.55).

## Maintaining Price Target at \$23

Our 12-month price target of \$23 is derived using a DCF analysis. This implies a 15.3x PE on our recurring 2006 EPS or in-line with peers, which we believe to be appropriate given our expectation that regulatory uncertainty will offset Puget's above average earnings growth potential.

Price movement to \$23 per share – when combined with the current \$1.00/share annual dividend (or 4.3% yield) – suggests a 4.1% total return potential.

## Key 2Q05 EPS Drivers

Puget Sound Energy (PSE), the utility, realized a recurring 2Q05 EPS of \$0.15, similar to what was achieved in 2Q04. Rising O&M expense (-\$0.06) led the drag on the company's results due to planned maintenance on the company-owned energy production facilities and delivery infrastructure. Higher depreciation and amortization expense (-\$0.02) was a result of investment in utility operations. The company expects its higher D&A trend to continue in 2005 and beyond as PSE invests in energy delivery and generation infrastructure to support its service territory growth as part of its Least Cost Plan.

Offsetting the drag was higher electric and gas customer growth of 1.9% and 3.2%, respectively. Higher energy sales volumes over 2Q04 due to cooler temperatures in the Pacific Northwest were a positive, although temperatures remained warmer than historical averages. The combination of a 4.9% retail KWh increase combined with a 4.1% rate increase, which took place March 4<sup>th</sup>, also buoyed results. The rate increase accounted for \$4.9 million, net of the Tenaska disallowance recorded in 2Q04. Gas margins also increased \$4.0 million during the quarter primarily due to a 10% rise in therm sales and the impact of a 3.5% natural gas rate increase, which also took effect on March 4<sup>th</sup>.

## ■ Puget Energy Inc.

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. InfrastruX provides infrastructure construction services to the electric and gas utility industries.

## ■ Statement of Risk

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.

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UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	40%	41%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	49%	43%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	35%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 30 June 2005.

### KEY DEFINITIONS

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

**Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

**Rating/Return Divergence (RRD)** This qualifier is automatically appended to the rating when stock price movement has caused the prevailing rating to differ from that which would be assigned according to the rating system and will be removed when there is no longer a divergence, either through market movement or analyst intervention.

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**UK and European Investment Fund ratings and definitions are:** Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Reduce: Negative on factors such as structure, management, performance record, discount.

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**Companies mentioned**

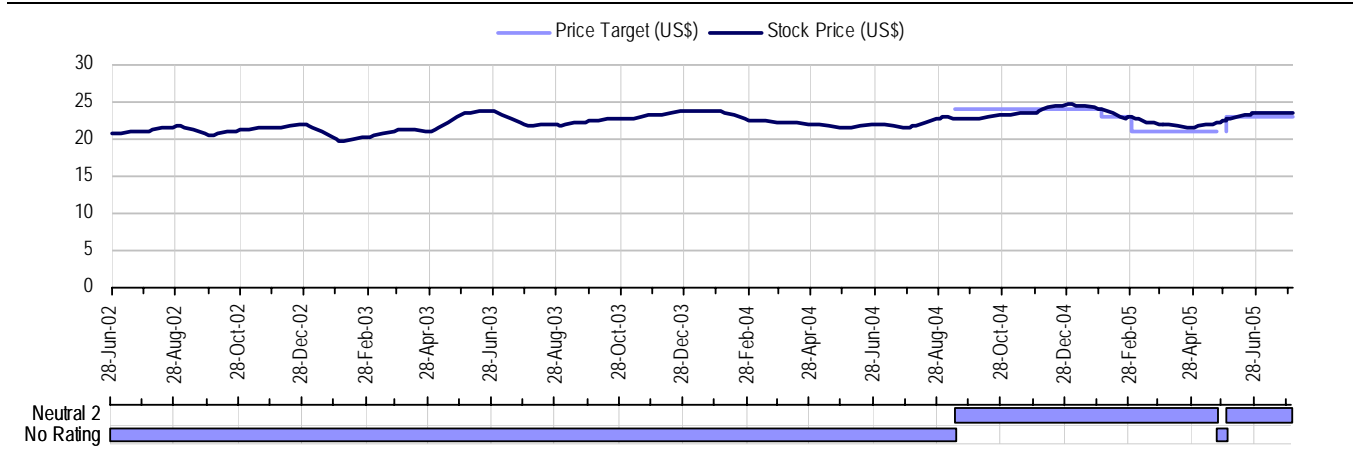
Company Name	Reuters	Rating	Price	Price date/time
<b>Puget Energy Inc.</b> <small>2,4,5,6a,6b,6c,7,16,18</small>	PSD.N	Neutral 2	US\$23.42	02 Aug 2005 19:36 EDT

Source: UBS. EDT: Eastern daylight time.

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Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

**Puget Energy Inc. (US\$)**



Source: UBS; as of 2 August 2005.

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# Puget Energy

## Reports Inline 2Q05 Results

- Puget Energy reported inline 2Q05 results; however, the company earns the bulk of its profits in 1Q and 4Q because it is a winter peaking utility. We are maintaining our Neutral rating on the shares.
- Puget reported 2Q05 earnings from ongoing operations of \$0.15 in line with our expectations, but ahead of consensus of \$0.11. The company benefited from higher customer sales volumes as well as higher results following the company's recent rate case. This was partially offset by higher operations and maintenance expenses due to the timing of planned maintenance.
- The company remains on track with its wind project development and it continues to work through its Power Cost Only Rate Case filing which will allow it to recover its wind project costs in rates. However, the company continues to suffer from a regulatory lag as it invests in its utility infrastructure, but is unable to recover its costs in rates.

**Neutral**

**\$23.37**

03 August 2005

### Electric Utilities

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### Puget Energy (PSD;PSD US)

	2004A	2005E	2006E
EPS (\$)			
Q1 (Mar)	0.67	0.70A	
Q2 (Jun)	0.16	0.15A	
Q3 (Sep)	0.11		
Q4 (Dec)	0.61		
FY	1.60	1.40	1.55
P/E FY	14.6	16.7	15.1

Source: Company data, Reuters, JPMorgan estimates.

### Company Data

Price (\$)	23.37
Date Of Price	03 August 05
52-week Range	20.73 - 24.81
Mkt Cap (\$ mn)	2,334.41
Fiscal Year End	Dec
Shares O/S (mn)	100
Div. Yield	4.3%

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## Valuation and Rating Analysis

We are maintaining our Neutral rating as Puget Energy appears to continue to struggle with regulatory lag and other factors that are preventing its core utility EPS power from emerging. We expected Puget to offer investors an attractive EPS growth profile, aided in part by a constructive regulatory outcome of the company's recent electric rate case. We believe the recent electric rate case was resolved constructively; however, the company appears to be continuing to struggle to realize the full potential of its earnings power as established in its recent rate case. Longer-term, we believe Puget still has the potential to offer investors an attractive EPS growth profile; however, it appears that the company's struggle to earn its allowed ROE will prevent the potential EPS growth from investing in its utility from emerging for at least the next several quarters. We expect the company's above-average dividend to support the shares, and the shares are trading just below the group average multiple of 15.8x 2006E EPS. Furthermore, if the company is able to address some of the issues masking its core utility earnings power, the shares appear attractively valued. For example, if the company is able to address \$0.15 of regulatory lag it is currently suffering by 2006, we estimate that the company could earn about \$1.70 in 2006, which would imply that the stock is trading at about 13.7x 2006E EPS, a significant discount to the group average 2006 multiple, especially given the company's above average yield. We believe this profile could ultimately prove attractive, but we expect the stock to trade inline with the group for the next several quarters because we do not believe visibility on potential EPS improvement will emerge over that time frame.

## Risks to Our Rating

Our Neutral rating on Puget shares is based on what we expect to be EPS dampened by regulatory lag and other factors for at least the next several quarters. This results in the company underearning its allowed ROE. If Puget continues to suffer from additional underearning pressure, or inability to add its planned utility investment to rate base, we would expect EPS, and thus the shares, to suffer. On the other hand, as we discussed above, if Puget is able to address its regulatory lag, we believe the shares appear attractive on a relative valuation. As we also discussed above, we expect visibility on this issue to take several quarters to emerge. If Puget is able to address its lag sooner rather than later, investors could get earlier visibility on higher EPS in 2006 and the shares could outperform.

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North America Equity Research  
 03 August 2005

## Companies Recommended in This Report

Puget Energy (PSD/\$23.37/Neutral)

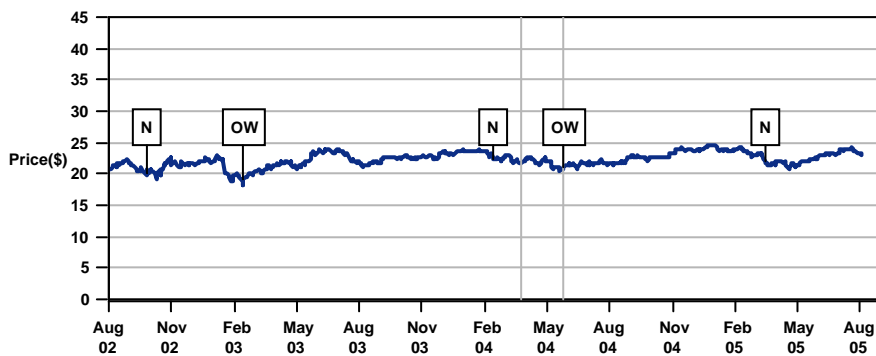
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Puget Energy (PSD) Price Chart



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.  
 Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.  
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Prior to September 25, 2002, our rating system was: Buy — we expect the stock to outperform the market by a minimum of 5% within an investment horizon of one year; Long-Term Buy — we believe the stock will outperform the market over the long run, but we lack the visibility of a catalyst for outperformance within a one-year investment horizon; Market Performer — the stock is expected to perform in line with the market; Market Underperformer — we expect the stock to underperform the market by a minimum of 5% within an investment horizon of one year.

Coverage Universe: **Andrew Smith:** American Electric Power (AEP), CMS Energy Corp (CMS), Calpine Corp. (CPN), Consolidated Edison (ED), Constellation Energy Group (CEG), Dominion Resources (D), Duke Energy (DUK), Entergy

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North America Equity Research  
03 August 2005

Corp. (ETR), Exelon Corp. (EXC), FPL Group Inc. (FPL), Puget Energy (PSD), Reliant Energy, Inc (RRI), Southern Company (SO), TXU Corp. (TXU), Wisconsin Energy Corp (WEC)

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	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	40%	42%	18%
IB clients*	47%	46%	39%
JPM SI Equity Research Coverage	34%	49%	17%
IB clients*	66%	57%	47%

\*Percentage of investment banking clients in each rating category.

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North America Equity Research  
03 August 2005

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Revised June 30, 2005.

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**North America Equity Research**  
03 August 2005

□  
Exhibit No. \_\_\_(BAV-5)  
Page 184 of 297

08.03.2005

Puget Energy, Inc. (PSD)

Solid Q2 Results

\$23.32 | BUY

- Puget Energy reported Q2 earnings of \$0.14 per share, beating the street consensus of \$0.12 per share.
- Wind farms remain on schedule, with the first, Hopkins Ridge, scheduled for completion in December.
- Fine tuning 2005 earnings estimate to \$1.36 from \$1.35. 2006 estimate remains \$1.48.
- PSD is rated Buy.

52 Week High	\$24.81
52 Week Low	\$20.73
P/E	15.1x
FY04A	17.2x
FY05E	15.8x
FY06E	
12 Mo. Price Target	\$26.00
Shares Out (Mil)	100.7
Market Cap (Mil)	\$2,348.3
Avg Daily Vol (000s)	242.6
Equity Ratio	41.8%
Book Value	\$16.52
Dividend	\$1.00
Yield	4.28%
3- 5 yr EPS Growth	3%
Fiscal Year End	Dec

EPS ESTIMATES

FY04A	\$1.55
FY05E	\$1.36
FY06E	\$1.48

▲ Puget Energy reported Q2 earnings per share of \$0.14, including \$0.12 per share of contribution from the core electric and gas utility, and \$0.02 per share of contribution from InfrastruX, the discontinued utility construction services subsidiary. The street estimate for the quarter was \$0.12. Earnings for the quarter included a \$0.03 expense to true-up previously reported gas costs, as well as higher utility depreciation and operation and maintenance (O&M) costs associated with regulatory lag.

PSD continues to move forward with its plan to increase its generation self-sufficiency. The company has broken ground on the 150 MW Hopkins Ridge wind power project and still anticipates completion in December of this year. A power cost only rate case for Hopkins Ridge was filed in June with the Washington Utilities and Transportation Commission (WUTC). Permits have been received on the 230 MW Wild Horse wind farm project, which remains scheduled for completion at the end of 2006. The company also recently filed requests for proposals (RFPs) with the WUTC on an additional 1500 MW of generation capacity to be purchased in the 2015 time frame.

The company continues to expect a sale of InfrastruX in 2005. In the meantime, the small profit reported in Q2 was generally in line with our expectations.

We have fine-tuned our 2005 earnings estimate to \$1.36 from \$1.35, adding a penny of the positive two cent surprise to our estimate. Note that earnings for the year include approximately \$0.15 per share of costs associated with regulatory lag (2/3 depreciation, 1/3 O&M). Our new estimate is in line with management guidance, which was reiterated at \$1.30—\$1.40 per share. We expect earnings in Q3, the seasonal low quarter, to be approximately breakeven. Our 2006 earnings estimate remains at \$1.48 per share. We believe these estimates are on the conservative side, and that surprise potential is more likely to come in the form of upside surprises over the next two years (especially given the recent completion of the general rate case).

We continue to remain generally favorable on the utility sector, despite a strong recent performance, given the possibility of increased industry consolidation in the wake of a repeal of the Public Utility Holding Company Act. In view of this and PSD's potential for modest upside earnings surprises, we continue to rate PSD Buy.

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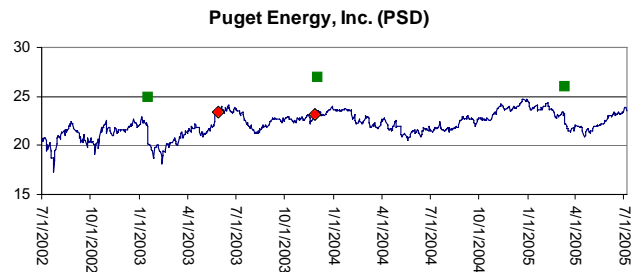
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As of June 30, 2005

	From	To	Date	Price
■	Price Target	\$27 to \$26	3/11/2005	\$22.25
■	Price Target	\$25 to \$27	12/1/2003	\$23.48
◆	Added to Focus List		11/26/2003	\$23.21
●	Hold to	Buy	11/26/2003	\$23.21
◆	Removed from Focus List		5/28/2003	\$23.40
●	Buy to	Hold	5/28/2003	\$23.40
■	Price Target	To \$25	1/16/2003	\$20.24



● Ratings Change ◆ Focus List Change ■ Target Price Change

Price targets are subject to change as new information becomes available, and reflect our current judgment regarding this security. Note that there are risks that may impede the achievement of a predicted price target. Price targets are based on fundamental factors such as historical and projected earnings, cash flow, discounted cash flow, relative book value, peer group evaluation, relative sector valuations, and expectations on general market and economic conditions.

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Hold/Addition to InStock Recommended List: We expect the Stock to be a Market Performer.

Sell/Removal from InStock Recommended List: We expect the Stock to Underperform the Market.

Ratings System in effect between 2/7/2002 and 6/12/2002: Strong Buy, Buy, Hold, Underperform, Sell.

Ratings System in effect prior to 2/7/2002: Buy, Moderate Buy, Hold, Underperform, Sell.

	Percentage of Rated Stocks Currently Assigned this Rating	Percentage of Rated Stocks with this Rating with which MWR has had an Investment Banking Relationship in the last 12 months
Buy	52%	6%
Hold	38%	8%
Sell	11%	0%

For Price Chart and Ratings History disclosures, please go to <http://www.mwrinc.com/ClientAccess/quotesresearch.html>, or to request information, please contact Jason T. Kunkel, Research Assistant, (206) 664-8854, [mwr@mwrinc.com](mailto:mwr@mwrinc.com)

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# Puget Energy, Inc.

## PSD: Lowering Rating to Market Perform on Valuations, Weather and Rate Increases Boost Q2 Results

**Summary:** PSD reported second quarter results of \$0.14 (\$0.19 after adjustments) compared to a loss of \$0.07 (\$0.18 after adjustment) the prior year. The results were essentially in line with the prior year after adjusting for Tenaska disallowances (\$0.25 the prior year and \$0.02 this quarter) and one-time PGA adjustment (\$0.03 this quarter). The Utility division reported EPS of \$0.12 (\$0.17 after adjustments) compared to a loss of \$0.10 (\$0.15 profit after adjustments). The InfrastruX division, which was classified as discontinued business, reported \$0.02 compared to \$0.03 the prior year. We are maintaining our FY'05 and FY'06 EPS estimates of \$1.36 and \$1.50, respectively. However, we are lowering our rating to Market Perform based on valuation

- **Total revenues increased 20.6% to \$510.0 million mainly due to rate increases.** Electric margins increased by \$42.7 million mainly due to lower Tenaska charges. Gas margins increased \$4.0 million primarily as a result of rate increases and cooler weather. Weather was 15% cooler than last year. Customer growth for the LTM ending June 2005 was 1.9% for electric and 3.2% for natural gas.
- **Operation and maintenance expenses increased 13.6% to \$83.1 million due to planned maintenance.** D&A increased approximately 5.5% to \$59.7 million due to infrastructure additions. Interest expense decreased less than a percent to \$41.5 million mainly due to lower interest debt.
- **InfrastruX reported \$0.02 compared to \$0.03 the prior year.** The Company intends to sell this division by the end of fourth quarter this year making it a 100% regulated utility. PSD had approximately \$34 million equity in this division at the end of the second quarter.
- **The Company has filed a power cost only rate case (PCORC) in June 2005 for a 3.7% increase of \$55.6 million increase in annual electric revenues.** This filing includes the recovery of investments in the Hopkins Ridge project, which is expected to go online in late 2005.

### Valuation

PSD stock is currently trading at 17.2x our FY'05 estimate of \$1.36 and 15.6x our FY'06 estimate of \$1.50, which is in line with the peer group average. On EV/EBITDA basis, the stock is trading at 7.5x or at a discount to the peer group average of 8.7x. On price-to-book basis, the stock is trading at 1.4x essentially in line with the peer group average of 1.5x. Its dividend yield is 4.3% compared to 3.6% peer group average. At the current price levels, we believe the stock is fairly valued. As a result, we are lowering our rating to Market Perform from Market Outperform.

### Regional Growth August 4, 2005

**Puget Energy Inc.**  
**PSD/NYSE**  
**Closing Price on 8/3/05: \$23.37**  
**Market Perform**  
**From Market Outperform**

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52-Week Range	\$20.73 – \$24.81
Average Daily Volume	306,094
Shares Outstanding	100.2 million
Market Capitalization	\$2.35 billion
Market Cap./2005E Revenue	1.0x
Long Term Debt (Mil)	\$2,306
Total Debt / Total Capitalization	58%
Institutional Ownership	49%
Trailing 12 mo. Revenue	\$2,359 million
Book Value per Share (06/05)	\$16.27
Long-Term Projected EPS Growth	5%
Dividend	\$1.00
Dividend Yield	4.3%

### Annual Estimates

FY (Dec)	2003A	2004A	2005E	2006E
Revs (Mil)	\$2,041	\$2,199	\$2,444	\$2,517
% chg y/y	2%	8%	11%	3%
<b>EPS</b>	<b>\$1.22</b>	<b>\$0.55*+</b>	<b>\$1.36</b>	<b>\$1.50</b>
Street	-	-	\$1.38	\$1.50
Price/EPS	19.2x	NMF	17.2x	15.6x

### Quarterly EPS Estimates

FY (Dec)	Mar	Jun	Sep	Dec
2005E	\$0.71A	\$0.14A	\$0.00	\$0.52
Street	-	-	\$0.04	\$0.55
2004A	\$0.67	(\$0.07)*	\$0.11	(\$0.16)+
2003A	\$0.45	\$0.22	\$0.10	\$0.45

\*Includes a \$0.28 charge related to Tenaska Order

+Includes a \$0.77 charge related to goodwill impairment

**Required Disclosures: C-2**  
**See Page 5 for Required Disclosures**

### Equity Research

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**Second Quarter Highlights**

PSD reported second quarter results of \$0.14 compared to a loss of \$0.07 the prior year. Of the \$0.14, Puget Sound Energy (PSE), the utility division, generated \$0.12, and InfrastruX, the discontinued, non-regulated division, contributed \$0.02. On the regulated side, the increase in earnings was mainly due to lower Tenaska disallowance – \$0.02 this quarter compared to \$0.25 last year. Electric margins increased \$4.9 million (net of Tenaska disallowances) mainly as a result of 4.9% higher volumes due to cooler weather and a 4.1% rate increase from the PCORC (recovery of Fredrickson investment) and the general rate case. A 10% increase in volumes due to cooler weather and a 3.5% rate increase from the general rate case were the main reasons for a \$4.0 million increase in gas margins during the quarter compared to the prior year period. Weather was 11% warmer than normal and 15% cooler than last year. During this quarter there were one time true-up costs that resulted in \$5 million (\$3.3 million after-tax) decrease in gas margins or \$0.03 per share. Customer growth continued to be above the national average at 1.9% on the electric side and 3.2% on the natural gas side. Operations and maintenance expenses increased 13.6% to \$83.1 million due to planned maintenance. D&A increased approximately 5.5% to \$59.7 million due to infrastructure additions. Taxes other than income taxes increased 18.7% to \$50.5 million due to higher revenues and property taxes. Operating income increased 69.8% to \$51.9 million. Interest expense decreased less than 1% to \$41.5 million due to lower interest rate debt. InfrastruX reported earnings of \$1.9 million, or \$0.02, compared to \$2.9 million, or \$0.03 during the prior year period. Net income was \$13.9 million compared to a loss of \$6.8 million last year, and the diluted shares outstanding were 1% higher compared to last year.

**InfrastruX**

As of the quarter end, PSD had approximately \$34 million in net equity and approximately \$160 million in net debt in its non-regulated business, InfrastruX. During the quarter, InfrastruX reported \$0.02 earnings compared to \$0.03 last year, essentially in line with expectations. The Company reiterated its intention to monetize this business by the end of this year. For the quarter, the division generated \$18 million in EBITDA compared to \$16.5 million last year. For the full year, the \$40-\$45 million EBITDA guidance remains unchanged. Assuming a 6-8 multiple would imply an equity value of \$80 to \$200 million. We would anticipate the Company reducing debt with the net proceeds pending any other uses.

**Balance Sheet**

Total Long-Term Debt at the end of December was \$2.3 billion or 58% of the total capital. The Company incurred approximately \$117 million in cap ex in Q2'05 and \$237 million for the first half 2005. PSD guided that its cap ex for 2005 will be approximately \$580 million, roughly \$200 million of which will be used on Hopkins Ridge wind power project. This cap ex is expected to be funded by a combination of debt and equity.

**Outlook**

The acquisition of Hopkins Ridge 160 MW Wind Project was completed in March 2005. PSE expects to spend approximately \$200 million on this project, of which, \$180 million would be to acquire and construct wind plant, \$10 to upgrade transmission systems and the balance to develop, transact and finance the project. Power will be delivered to PSE's territory via the Bonneville Power Authority's transmission systems. The construction is expected to end in December this year. Another letter of agreement for the acquisition of Wild Horse Project in Kittitas County has been signed.

A power cost only rate case (PCORC) was filed in June 2005 requesting a 3.7% increase or \$55.6 million in annual electric revenues. This case includes the recovery of capital and anticipated operating costs for the Hopkins Ridge project. A final decision is expected in five months from the date of filing. The Company continues to increase its customer base above the national average. Customer growth for the LTM ended June 30, 2005 was 1.9% and 3.2% on electric and natural gas side. We view the divestment of the non-regulated portion of the business a positive, as it would make PSD a 100% regulated utility and aid the repayment of a portion of its debt from the sales proceed.

The Company maintained its earlier guidance of \$1.30-\$1.40 for FY 2005 and \$1.40-\$1.55 for FY 2006. The reason for maintaining guidance despite good performance in the 2005 (\$0.85 EPS YTD), was normal weather assumption in Q3 and Q4 this year. In FY'04, Q3 and Q4 experienced abnormally favorable weather. Q3'05 is expected to break even on normal weather assumptions. As a result, we are maintaining our FY'05 EPS estimate at \$1.36 and reducing our Q3 and Q4 estimates to fall within the range. We are estimating break even for Q3 and \$0.51 for Q4. We are also maintaining our FY'06 estimate of \$1.50 until we hear more on the acquisition of new generation resources and the PCORC.

**Valuation**

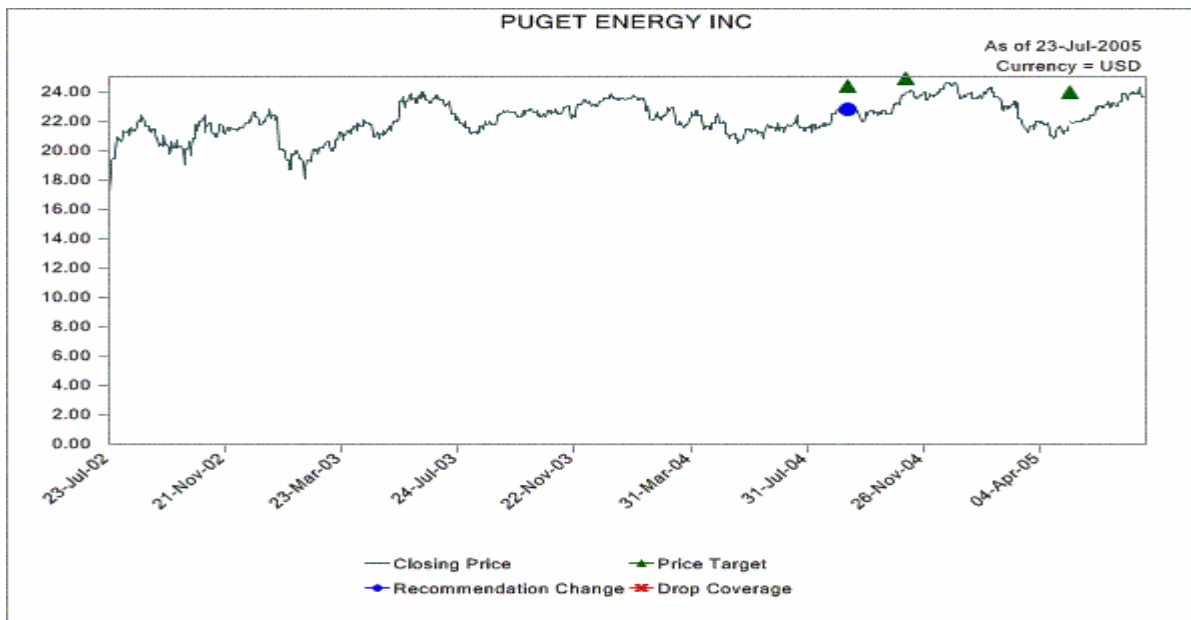
PSD stock is currently trading at 17.2x our FY'05 estimate of \$1.36 and 15.6x our FY'06 estimate of \$1.50, which is in line with the peer group average. On EV/EBITDA basis, the stock is trading at 7.5x or at a discount to the peer group average of 8.7x. On price-to-book basis, the stock is trading at 1.4x essentially in line with the peer group average of 1.5x. Its dividend yield is 4.3% compared to 3.6% peer group average. At current price levels, we believe the price essentially reflects the growth opportunities. However, we would note that the PCORC could prove a positive catalyst in the short run. In the long run, the addition of low cost wind power in its portfolio could provide cost advantage to the Company. For now, we are lowering our rating to Market Perform from Market Outperform and would be more bullish on any pull back.



# Required Disclosures

Exhibit No. \_\_\_(BAV-5)

EFFECTIVE NOVEMBER 13, 2002, STIFEL NICOLAUS ELIMINATED PRICE TARGETS ON PERFORM-RATED STOCKS. ALL MARKET OUTPERFORM AND MARKET UNDERPERFORM-RATED STOCKS CONTINUE TO HAVE PRICE TARGETS.



**PUGET ENERGY INC**

Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
09-Sep-2004	22.88	MARKET OUTPERFORM	04-May-2005	21.77	24.00
			08-Nov-2004	24.05	25.00
			09-Sep-2004	22.88	24.50

*We, the research analysts responsible for this report, attest that the views expressed in this research report accurately reflect our personal views about any and all of the subject securities or issuers. We have not received, and will not receive, compensation in return for the specific recommendations or views expressed by us in this report.*

**KEY FOR DISCLOSURES:** A – Stifel, Nicolaus makes a market in the common stock of this company. B – The analyst owns the common stock of this company. B-1 – A member of the analyst’s household owns the common stock of this company. C – Stifel, Nicolaus has managed or co-managed a public offering of securities for this company within the past 12 months. C-1 – Stifel, Nicolaus has been compensated for investment banking services by this company within the past 12 months. C-2 – Stifel, Nicolaus intends to seek compensation for investment banking services from this company in the next 3 months. D – The analyst serves on the Board of Directors of this company. D-1 – A member of the analyst’s household serves on the Board of Directors of this company. E – Stifel, Nicolaus beneficially owns in excess of 1% of a class of common equity securities of this company.

**RATING SYSTEM:** Market Outperform – The total return of the stock, adjusted for risk, is expected to outperform the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Perform – The total return of the stock is expected to perform in line with the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Underperform – The total return of the stock is expected to Underperform the broad U.S. equity market, defined as the Russell 2000, over the next 12 months. The security should be sold if such sale is consistent with clients' needs and objectives. Our 12-month price targets may temporarily vary from these expectations due to market volatility.

**RESEARCH COVERAGE:** As of June 30, 2005, Stifel Nicolaus had 214 companies under coverage. Stifel Nicolaus rated 98 companies, or 45.8%, as Market Outperform/“Buy,” 115 companies, or 53.7%, as Market Perform/“Hold,” and 1 company, or 0.5%, as Market Underperform/“Sell.” During the previous 12 months, Stifel Nicolaus provided investment banking services for 17 of the companies rated Market Outperform/“Buy” (17%), 16 of the companies rated Market Perform/“Hold” (14%), and none of the companies rated Market Underperform/“Sell” (0%).

The information and statistical data contained herein have been obtained from sources we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to any changes in figures or our views.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST. Please contact the analyst for further information. Stifel, Nicolaus & Company, Inc. research is also available online at [www.multex.com](http://www.multex.com) and [www.firstcall.com](http://www.firstcall.com).

This is not a solicitation of any order to buy or sell.



AUGUST 4, 2005

UTILITIES

# Puget Energy, Inc.

NYSE-PSD

## 2Q05 Results In-Line

 ANALYST OPINION: **SELL**

### PRIMARY STOCK STATISTICS

FY End	Dec
52-Week Range	\$25-\$21
Market Cap (billion)	\$2.34
TTM Revenue (billion)	\$2.64
Shares Outstanding (million)	100.1
Book Value	\$15.96
Dividend/Yield	\$1.00/4.3%
Est. Sec. EPS Grth Rate	5%

 PRICE: **\$23.42**

 PRICE TARGET: **NA**

### EARNINGS ESTIMATES

Current Quarter

PRIOR
CURRENT
P/E

FY03A

-

\$1.22

19.2 x

FY04A

-

\$1.26

18.6x

FY05E

\$1.35

\$1.35

17.3x

### KEY POINTS

- PSD reported 2Q05 normalized EPS of \$0.15 (includes one time \$0.03 gas true up charge) which is the same as 2Q04.
- InfrastruX earned \$0.02 per share but shows up in discontinued operations as the company still expects the property to be monetized in 2005.
- Management reiterated FY05 guidance at between \$1.30 and \$1.40.
- We are maintaining our Sell rating as we believe there is little earnings leverage here although the dividend is attractive. With a forward PE of 17x, equity dilution seen likely over the next two years, and a high estimated dividend payout of almost 75%, we continue to feel better yield/growth opportunities lie in names like Exelon.

### SUMMARY AND STOCK OPINION

PSD reported 2Q05 EPS of \$0.15 when we add back a one time true up charge of \$0.03. This is the same as last year's 2Q. Rate increases of 4.1% for electricity and 3.5% for gas and strong electric and gas customer growth of 1.9% and 3.2% respectively were largely offset by a \$9.9 million increase in maintenance on owned production facilities and delivery infrastructure and increasing depreciation levels at company owned generation facilities.. We expect the trend towards higher O&M and depreciation expenses to continue for the foreseeable future.

Debt to capital at 57%, while improving from 60% at the end of 2004, is still high and the company is short generation capacity with much in the way of new investment required over the next many years to increase self reliance. The dividend payout is high given investment needs and the regulatory environment is fair.

We are holding off initiating a FY06 estimate for now.

Trading at 17x our FY05 estimate, a premium to the group probably due to the attractive yield, we feel the stock is somewhat overvalued here.

(Continued)

Peer Comparison

	Ticker	Price	Div. Yield (%)	P/Book	P/Sales	P/EBITDA	P/E (ttm)	P/E (est'05)
Pinnacle West Capital Corp.	PNW	\$46.39	4.1	1.4	1.5	4.6	17.4	15.0
Xcel Energy Inc.	XEL	\$19.52	4.4	1.5	0.9	4.2	16.4	15.8
Sempra Energy	SRE	\$42.90	2.7	1.9	1.0	5.3	11.2	13.2
Avista Corp.	AVA	\$19.39	2.8	1.2	0.8	4.1	28.7	19.1
PNM Resources Inc.	PNM	\$29.65	2.7	1.6	1.1	6.5	23.4	18.2
MDU Resources Group Inc.	MDU	\$30.93	2.3	2.2	1.2	5.8	15.4	15.2
AVERAGE			3.2	1.6	1.1	5.1	18.8	16.1
Dow Utilities Index	^UTIL	\$405.27	3.0	2.5	1.4	NA	19.9	16.9
<b>Puget Energy Inc.</b>	<b>PSD</b>	<b>\$23.42</b>	<b>4.3</b>	<b>1.4</b>	<b>1.0</b>	<b>3.6</b>	<b>38.8</b>	<b>16.8</b>

Puget Energy, Inc. is one of Washington state's largest utility companies. Through its subsidiary, Puget Sound Energy, it provides electricity to more than 940,000 customers and provides natural gas to more than 600,000 in western Washington. The company owns some fossil-fueled and hydroelectric plants and its InfrastruX Group specializes in energy management and infrastructure construction services. Headquarters: Bellevue, WA

*Other public companies mentioned:*

Exelon Corporation. (NYSE-EXC-\$54.33, VLI-Hold)

**S&P 500: 1245.04**

**REQUIRED DISCLOSURES**

The analyst or a member of the analyst’s household has beneficial ownership in the securities of Puget Energy, Inc. in the form of a long position in such securities.

**ANALYST CERTIFICATION**

By issuing this research report, each Ragen MacKenzie analyst whose name appears on the front page of this research report hereby certifies that: (i) the recommendations and opinions expressed in the research report accurately reflect the research analyst’s personal views about any and all of the subject securities or issuers discussed herein and (ii) no part of the research analyst’s compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in the research report.

**PRICE TARGET VALUATION METHODOLOGY AND RISKS**

The methods used to determine the price target are generally based on a multiple of earnings, cash flow, revenue and/or historical and relative valuation multiples. Risks that could impede achievement of our price target include, but are not limited to, changes in economic and industry conditions, consumer and business spending patterns, as well as geo-political risks. When a price target is used, please refer to the Valuation and Risks section in the body of the report for additional discussion on the specific valuation methodology and related risk factors as they pertain to this analyst’s investment thesis.

**RATING SYSTEM**

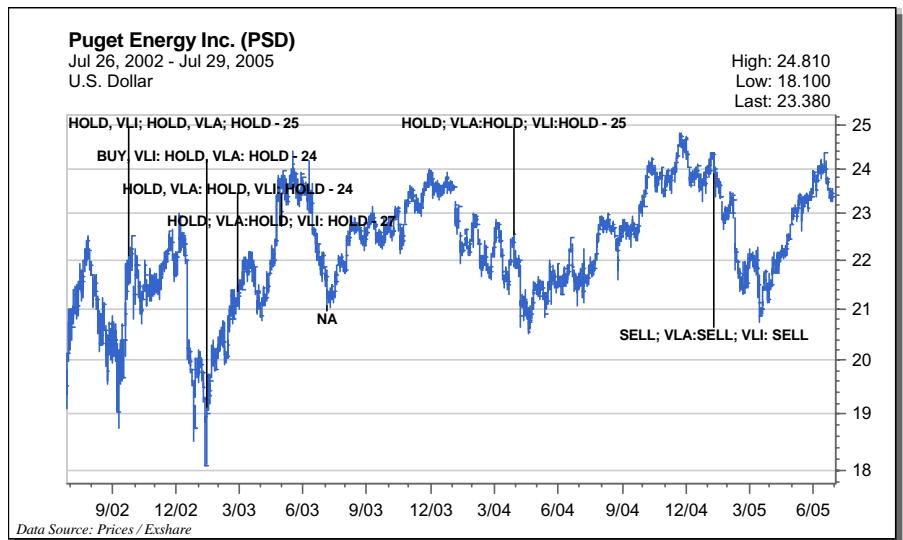
**BUY** – Immediate purchase is recommended; the stock is expected to outperform the general market over the next 12-18 months.  
**HOLD** – Holding the stock is recommended. The stock has moved out of our preferred buying range, but there is further upside to the share price; or stated objectives at the time of purchase have changed and share appreciation may take another 6-12 months.  
**SELL** – The stock has reached the stated price objective and appreciation has been achieved; or certain company fundamentals have changed which warrant investors selling the stock to avoid price decline.

**RATINGS ALLOCATIONS**

Rating	% of covered companies with this rating	% for which IB Services have been provided
<i>Analyst Coverage</i>		
BUY	26%	0%
HOLD	69%	5%
SELL	6%	0%
<i>Value Recommended List—Appreciation</i>		
BUY	38%	0%
HOLD	54%	0%
SELL	8%	0%
<i>Value Recommended List—Income</i>		
BUY	33%	50%
HOLD	67%	25%
SELL	0%	0%
<i>Growth Recommended List</i>		
BUY	33%	0%
HOLD	50%	0%
SELL	17%	0%

Updated on 07/11/2005

**PRICE HISTORY**



The price targets indicated in the chart above may be adjusted for stock splits. Where the price target was originally given as a range, the midpoint of the range has been used. Until July 8, 2002, Ragen MacKenzie used the following system for analyst ratings: Strong Buy (SB), Buy, Market Perform (MP), Underperform, Sell. The current rating system, explained above, has been in effect since July 9, 2002.

**OTHER DISCLOSURES**

**INVESTMENT PRODUCTS:**   ▶ **NOT FDIC INSURED**   ▶ **NO BANK GUARANTEE**   ▶ **MAY LOSE VALUE**

**Additional Information on Subject Companies Mentioned Herein Is Available Upon Request.** Ragen MacKenzie is a division of Wells Fargo Investments, member SIPC, a non-bank affiliate of Wells Fargo & Co. This is not a complete analysis of every material fact regarding any company, industry, or security. The information has been obtained from sources we consider to be reliable, but we cannot guarantee the accuracy. Opinions represent the analyst’s judgment as of the date of the report and are subject to change without notice. Ragen MacKenzie may have issued, and may in the future issue, other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. WFI affiliates may issue reports or have opinions that are inconsistent with and reach different conclusions from this report. Those reports reflect different assumptions, views and analytical methods of the analysts who prepared them, and neither WFI nor its affiliates are under any obligation to ensure that such other reports are brought to the attention of any recipient of this report.

**PUGET ENERGY, INC.**

PSD – NYSE

August 26, 2005

**Rating:****NEUTRAL****Price:** (8/25/05) \$22.64**Price Targets:**

12-18 month: \$23

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

406.791.7230

jbellessa@dadco.com

FY (Dec)	2004A*	2005E**	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,198.9	\$2,480.8	13%	\$2,572.1	4%
Previous		\$2,414.7		\$2,514.4	
Price/Revenue ratio	1.0x	.9x		.9x	
<b>EPS Revised</b>	<b>\$0.55</b>	<b>\$1.44</b>	162%	<b>\$1.48</b>	3%
Previous		NC		NC	
Price/EPS ratio	41.1x	15.7x		15.3x	
<b>EBITDA (\$M)</b>	\$597.4	\$637.0	7%	\$704.1	11%
EV/EBITDA ratio	8.0x	7.5x		6.8x	

Quarterly Data:	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05A**	<b>\$0.71</b>		\$741.7	\$801.5	\$215.9
6/30/05A**	<b>\$0.14</b>	\$0.15	\$510.1	\$456.8	\$119.3
9/30/05E**	<b>\$0.04</b>	NC	\$449.5	\$436.8	\$104.1
12/31/05E	<b>\$0.55</b>	\$0.56	\$779.6	\$779.4	\$197.8

\*See detail of footnotes on page 2. \*\* Includes \$0.05 per share from discontinued operations in 2005, including (\$0.01) in 1Q'05, \$0.02 in 2Q'05, and \$0.04 in 3Q'05.

**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (6/30/05)	60.5%
Cash per share (6/30/05)	\$0.18
Book value per share (6/30/05)	\$16.58
Dividend (yield)	\$1.00 (4.4%)
Return on Equity (T-T-M)	5%

**Trading Data**

Shares outstanding (M)	100.3
Market Capitalization (\$M)	\$2,270
52-week range	\$20.73 - \$24.81
Average daily volume (3 mos.) (K)	288
Float	99%
Index Membership	S&P 400 MidCap

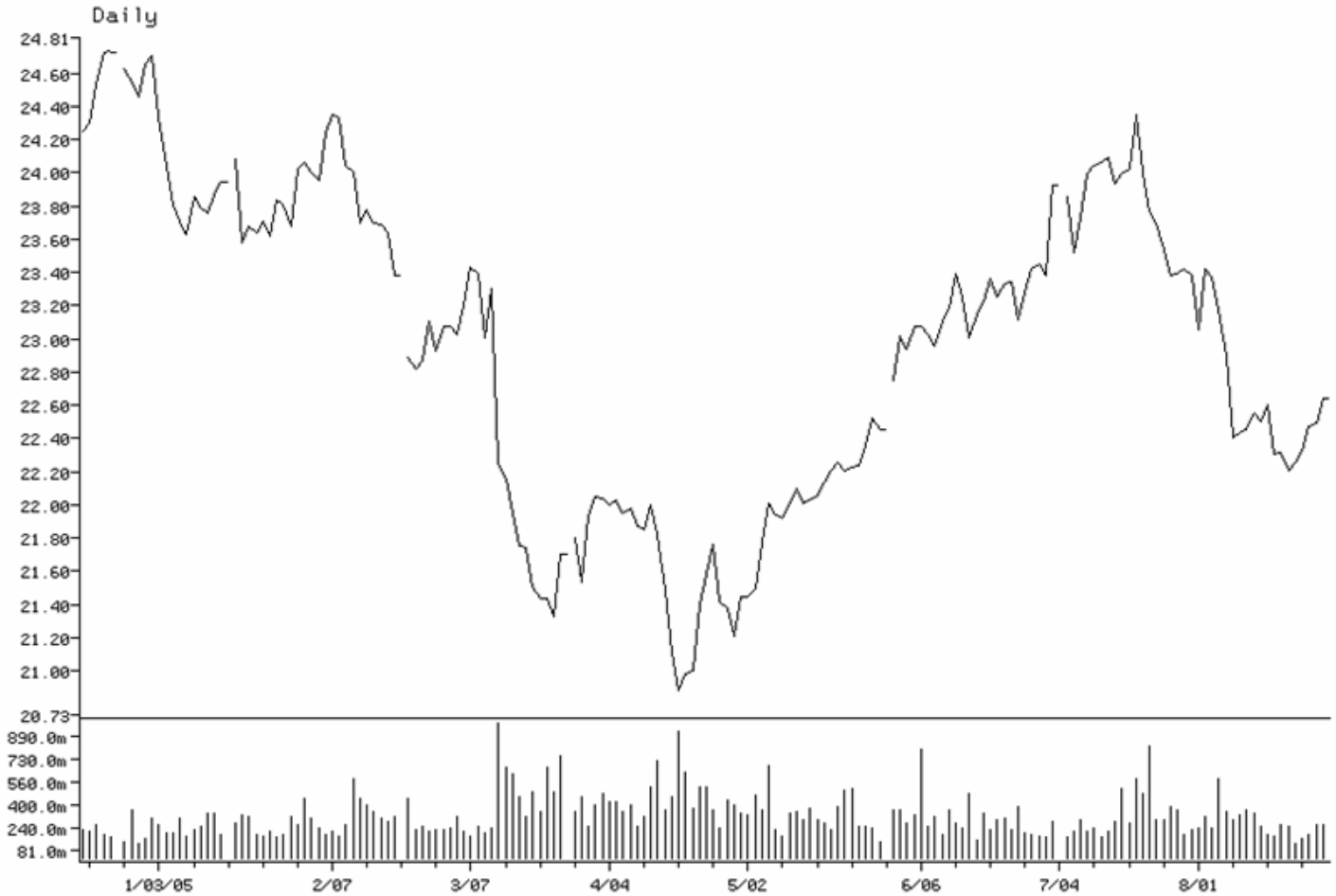
**Maintaining EPS Estimates as Quarterly Results Match Forecast.  
Target Price and NEUTRAL Rating Remain Unchanged.**

- On August 2, Puget Energy reported 2Q'05 diluted EPS of \$0.14, compared to a loss of \$0.07 for 2Q'04. We were forecasting \$0.15.
- Hurting the recent quarter's results were a \$0.03 per share true-up of previously reported gas costs, which was not expected, and a \$0.02 per share charge for on-going Tenaska plant-related disallowances, which was anticipated.
- We are maintaining our 2005 EPS estimate of \$1.44, although the earnings contribution of the utility and InfrastruX are being modified slightly. Our 2006 EPS estimate remains unchanged.
- Our 2005 EPS estimate for the utility is being lowered from \$1.42 to \$1.39, and our forecast for InfrastruX is being raised from \$0.02 to \$0.05. Our previous forecast of a mid-2005 divestiture of this discontinued operation was not achieved, and hence we now expect a 3Q'05 contribution from this utility service business. Cooler temperatures and higher expenses than we previously forecasted should leave 3Q'05 utility results near breakeven.
- We are maintaining our 12-18 month target price of \$23, or 15.5x our 2006 EPS estimate. Over the past decade, the stock of PSD has traded at a median 13.0x multiple of year-forward earnings. With the share price near our target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.4%.

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*Includes a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

\*\*Includes 1Q'05 benefit of \$0.04/sh. for partial recovery of a previously reported regulatory disallowance related to the Tenaska gas supply regulatory asset and on-going disallowance of approximately \$0.02/sh. Includes 2Q'05 charges of \$0.02/sh for regulatory Tenaska disallowance and \$0.03/sh. for the true-up of previously reported gas costs.

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**Operating Results Match  
Expectations**

On August 2, Puget Energy reported 2Q'05 diluted EPS of \$0.14, compared to a loss of \$0.07 for 2Q'04. We were forecasting \$0.15.

Hurting the recent quarter's results were a \$0.03 per share true-up of previously reported gas costs, which was not expected, and a \$0.02 per share charge for on-going Tenaska plant-related disallowances, which was anticipated. The loss a year ago was generated when the utility posted a \$0.25 per share after-tax regulatory disallowance for Tenaska plant-related issues.

Now reported as discontinued operations, InfrastruX contributed \$0.02 per share to 2Q'05 earnings, compared to \$0.03 per share a year ago and our projection of \$0.03 per share. Puget is attempting to monetize its investment in this business through a sale or third party recapitalization. While the amount InfrastruX will be divested for is uncertain, Puget says the sales proceeds will be invested in the regulated utility. Also, the timing of the InfrastruX divestiture is uncertain. Management has said it should be consummated before year-end 2005. Our earnings model now assumes divestiture at the end of 3Q'05, with an earnings contribution in the current quarter of \$0.04 per share and \$0.05 for the first nine months of 2005.

**Utility Incurred a True-Up Charge**

Utility 2Q'05 EPS of \$0.12 matched our forecast, and compared to last year's loss of \$0.10 per share stemming from the Tenaska disallowance.

Removing one time items, including the aforementioned true-up of gas costs, utility results for both periods were \$0.15 per share. During the recent quarter, management discovered that a gas demand charge for a gas customer rate class had not been included under the purchased gas adjustment (PGA) mechanism for the 31-month period between September 1, 2002 and March 31, 2005. To correct the overstatement of the PGA mechanism receivable, the company took a \$5.0 million charge, which after tax amounted to \$3.3 million, or \$0.03 per share, for the quarter ended June 30, 2005.

**Cooler Temperatures Combine  
With Customer Growth**

Quarterly electric revenues of \$345 million climbed \$42 million, or 14%, primarily due to a \$36 million increase in electric retail sales and a \$6 million increase in electric wholesale sales. The electric retail increase was aided by rate increases and higher retail customer usage. The increase in sales to other utilities and marketers was due to a 59% increase in megawatt-hour (Mwh) volumes related to excess generation available for sale on the wholesale market.

Retail sales rose \$22.0 million due a strong 4.9% increase in Mwh sales, as 1.9% customer growth combined with higher usage due to temperatures that were 15% cooler than a year ago. Retail sales rose an additional \$14 million because of the May 24, 2004 rate increase for the rate basing of the company's one-half interest in the Fredrickson plant and the March 4, 2005 general rate increase for utility services.

After deducting the costs of generating and purchasing electric energy from electric revenues, Puget Sound Energy had electric margins of \$151 million during 2Q'04. These electric margins were up \$43 million, or 39%, primarily because of the absence of last year's \$38 million in Tenaska plant related disallowances. Also helping the electric margin were the aforementioned electric rate increases and customer growth. These electric margin beneficiaries were partially offset by the on-going \$3 million pretax regulatory disallowance in connection with gas supply costs for the Tenaska generating project.

Quarterly gas revenues of \$163 million rose \$43 million, or 36%, primarily due to higher tariffs under the current Purchased Gas Adjustment mechanism to recover higher purchased gas costs. Gas revenues also rose due to a 3.2% increase in customer growth, an improved economy in the company's service territory in Washington, and cooler temperatures that increased volumes even though consumers are curtailing usage in response to higher natural gas prices. Heating-degree days from April 1, 2005 through June 30, 2005 in the company's service territory were 15% cooler than a year earlier but 11% warmer than normal. After

deducting the costs of gas sales, to retail and transportation customers, from gas revenues, gas margins were \$46 million in 2Q'05, which were up \$4.0 million, or 10%, from 2Q'04.

**EPS Forecasts Remain Unchanged**

Management reiterated 2005 EPS guidance of \$1.30-\$1.40, but did not say whether its 2006 EPS guidance of \$1.40-\$1.55 had changed.

We are maintaining our 2005 EPS estimate of \$1.44, but modifying our contributions from the utility and InfrastruX. Our 2005 EPS estimate for the utility is being lowered from \$1.42 to \$1.39, and our forecast for InfrastruX is being raised from \$0.02 to \$0.05 as our previous forecast of a mid-2005 divestiture was not achieved. For the utility, third quarter temperatures appear to be milder than last year, which will likely pinch electric and gas margins, and expenses for operations and maintenance are likely to be higher than we previously forecasted. For the year, the utility continues to face a 2005 regulatory lag of recovering rising costs not reflected in the March 4, 2005 rate order (-\$0.15 per share) and on-going disallowances of certain Tenaska gas costs (-\$0.07 per share). If our utility EPS forecast of \$1.39 is attained, it would fall into the \$1.30-\$1.40 range provided by management.

Our 2006 EPS forecast is being maintained at \$1.48, up 6% from our 2005 comparable figure of \$1.39. Note: our 2006 projection of a 13% increase in consolidated net income from continuing operations is being diluted by a 6% increase in average shares outstanding, chiefly because of our assumption of a year-end 2005 offering of approximately 5.0 million shares to help finance capital expenditures, especially for two wind power projects. The \$200 million Hopkins Ridge wind project, with 150 MW of capacity, or 52 average MW, should be in operation by year-end 2005. The \$350 million Wild Horse wind project, with approximately 230 MW of capacity, or 77 average MW, should be operating by year-end 2006.

On June 7, 2005, the utility filed a power cost only rate case (PCORC) with the Washington Utilities and Transportation Commission (WUTC) to help recover the higher cost of power, including the costs of the Hopkins Ridge wind power project. The company is requesting a \$55.6 million, or 3.7%, increase in electric rates. A WUTC decision for the PCORC is expected in November. While we are not specifically forecasting the outcome of the case, especially since the 3-member WUTC is comprised of two new members which are yet to conclude a rate case, we are projecting that electric rates in 2006 will be 2.5% above their average 2005 levels.

**Maintaining Target Price and  
NEUTRAL Rating**

We are maintaining our 12-18 month target price of \$23, or 15.5x our 2006 EPS estimate. Over the past decade, the stock of PSD has traded at a median 13.0x multiple of year-forward earnings. With the share price near our target, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock is the current yield of 4.4%.

James L. Bellessa Jr., CFA  
Vice President, Senior Research Analyst  
406.791.7230

## PUGET SOUND ENERGY, INC.

## BALANCE SHEET

(\$000's; years end 12/31)

	2000	2001	2002	2003	6/30/2004	2004	6/30/2005
<b>Assets</b>							
<b>Utility Plant:</b>							
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,326,999	\$4,389,882	\$4,495,814
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,806,799	1,881,768	1,937,595
Common plant	351,051	362,670	378,844	390,622	402,869	409,677	416,119
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,386,239)	(2,452,969)	(2,522,339)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,150,428	4,228,358	4,327,189
<b>Other Property and Investments:</b>							
Total other property and investments	292,297	317,249	378,130	402,093	402,830	157,670	159,085
<b>Current Assets:</b>							
Cash	36,383	92,356	176,669	27,481	17,330	12,955	16,616
Restricted cash			18,871	2,537	1,842	1,633	1,105
Accounts receivable, net							
Less: Allowance for doubtful accounts							
Total accounts receivable	343,108	279,321	279,623	227,115	136,262	137,659	203,523
Unbilled revenues	211,784	147,008	112,115	131,798	68,084	140,391	73,295
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	99,046	97,578	98,380
Purchased gas receivable	96,050	37,228			9,747	19,088	32,563
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	22,833	14,791	37,171
Taxes receivable							
Prepayments and other	11,607	11,277	11,323	12,200	17,531	8,273	18,037
Current assets of discontinued operations						110,922	116,670
Total current assets	797,933	660,838	672,744	493,852	372,675	543,290	597,360
<b>Long-Term Assets:</b>							
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	138,540	127,252	138,347
PURPA buyout costs	243,071	244,635	243,584	227,753	219,497	211,241	201,205
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	15,683	21,315	29,600
Power cost adjustment mechanism				3,605			5,518
Other	177,609	239,941	269,876	315,739	377,865	401,795	389,856
Long-term assets of discontinued operations						160,298	164,990
Total Long-term assets	628,030	680,909	690,388	698,513	751,585	921,901	929,516
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,677,518</b>	<b>\$5,851,219</b>	<b>\$6,013,150</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>							
Common stock	\$859,038	\$870	\$936	\$991	\$995	\$999	\$1,003
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,612,990	1,621,756	1,630,524
Earnings reinvested in the business	92,673	32,229	36,396	58,217	68,212	13,853	48,842
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(3,030)	(14,332)	(17,557)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,679,167	\$1,622,276	\$1,662,812
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250	280,250	237,750
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,105,272	2,069,360	2,073,360
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,066,578	3,973,775	3,975,811
Minority interest in equity of a consolidated subsidiary			10,629	11,689	11,959	4,648	5,346
<b>Current Liabilities:</b>							
Accounts payable	410,619	167,426	205,619	214,357	151,910	226,478	146,537
Short-term debt	378,316	348,577	47,295	13,893	52,415		159,623
Current maturities of long-term debt	19,000	119,523	73,206	246,829	60,049	31,000	77,000
Purchased gas liability	0	0	83,811	11,984			
Accrued expenses:							
Taxes	103,996	70,708	62,562	77,451	63,945	81,315	97,440
Salaries and wages	17,445	14,746	11,441	12,712	13,316	13,829	14,310
Interest	43,955	42,505	37,942	32,954	31,648	29,005	28,045
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636		26,581	13,948
Tenaska disallowance reserve					13,642	3,156	0
Other	26,685	46,178	47,761	46,378	53,172	34,918	32,472
Current liabilities of discontinued operations						51,892	61,232
Total current liabilities	1,000,016	844,808	572,047	660,194	440,097	498,174	630,607
Deferred Income Taxes	608,185	605,315	730,675	755,235	776,775	795,291	799,760
Other Deferred Credits	132,869	196,339	267,458	340,893	382,109	395,236	419,319
Commitments and Contingencies	0	0	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	0	385	83
Long-term liabilities of discontinued operations						183,710	182,224
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,677,518</b>	<b>\$5,851,219</b>	<b>\$6,013,150</b>

**% of Capitalization**

Total debt and mandatory redemption preferred	64.7%	67.4%	62.3%	60.3%	59.8%	59.5%	60.5%
Preferred stock	1.4%	1.4%	1.4%	0.0%	0.0%	0.0%	0.0%
Common stock	33.9%	31.2%	36.3%	39.7%	41.3%	40.5%	41.8%
	100.0%	100.0%	100.0%	100.0%	101.1%	100.0%	102.3%

## Shares outstanding (000's)

85,904	87,023	93,643	99,074	99,487	99,868	100,286
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## Book value per share

\$16.61	\$15.66	\$16.27	\$16.71	\$16.88	\$16.24	\$16.58
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## PUGET ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)

## OPERATING REVENUES:

	2003	1Q04	2Q04	3Q04	4Q04**	2004**	1Q05	2Q05	3Q05E	4Q05E	2005E	2006E
Electric	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$ 1,423,034	\$420,090	\$345,420	\$349,126	\$443,593	\$1,558,229	\$1,608,239
Gas	634,230	275,692	119,479	89,432	284,703	769,306	321,129	162,567	99,870	335,465	919,031	961,883
Other	<u>6,043</u>	<u>527</u>	<u>553</u>	<u>2,925</u>	<u>2,531</u>	<u>6,537</u>	<u>434</u>	<u>2,127</u>	<u>500</u>	<u>500</u>	<u>3,561</u>	<u>2,000</u>
Total operating revenues	<u>2,041,016</u>	<u>668,714</u>	<u>423,123</u>	<u>415,026</u>	<u>692,012</u>	<u>2,198,877</u>	<u>741,653</u>	<u>510,114</u>	<u>449,496</u>	<u>779,558</u>	<u>2,480,821</u>	<u>2,572,122</u>

## OPERATING EXPENSES:

## Energy costs:

Purchased electricity	714,469	196,367	173,847	147,589	205,764	723,567	208,178	178,943	165,486	224,014	776,621	751,852
Purchased gas	327,132	162,407	63,703	44,574	180,618	451,302	201,744	98,142	54,969	224,693	579,548	599,734
Electric generation fuel	64,999	13,988	21,014	25,130	20,640	80,772	20,448	12,894	26,184	26,616	86,142	88,453
Residential Exchange	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(55,046)	(37,105)	(34,214)	(50,570)	(176,935)	(175,000)
Unrealized (gain)/loss on derivative instruments	106	(87)	(2,849)	1,894	516	(526)	509	(591)	0	0	(82)	0
Utility operations and maintenance	289,702	73,855	73,201	67,093	77,083	291,232	75,522	83,132	80,000	81,000	319,654	329,000
Other operations and maintenance	1,547	484	500	484	741	2,324	741	558	500	500	2,299	2,000
Depreciation and amortization	220,087	55,870	56,569	57,598	58,529	228,566	58,077	59,657	61,000	64,000	242,734	264,000
Merger and related costs/conservation amort.	33,458	8,190	4,809	4,747	4,942	22,688	5,162	5,951	5,000	5,000	21,113	22,000
Goodwill Impairment												
Taxes other than federal income taxes	194,857	64,224	42,550	42,756	59,575	208,990	69,700	50,521	48,000	71,000	239,221	252,000
Federal income taxes	<u>70,775</u>	<u>39,097</u>	<u>(5,434)</u>	<u>6,957</u>	<u>36,134</u>	<u>76,757</u>	<u>46,084</u>	<u>6,093</u>	<u>210</u>	<u>32,720</u>	<u>85,107</u>	<u>95,095</u>
Total operating expenses	1,743,292	559,972	392,548	364,808	593,868	1,911,199	631,119	458,195	407,135	678,974	2,175,423	2,229,134

## OPERATING INCOME

## OTHER INCOME

## INCOME BEFORE INTEREST CHARGES

## INTEREST CHARGES, net of AFUDC

## Mandatorily redeemable securities interest

## Preferred stock dividends of subsidiary

## INCOME FROM CONTINUING OPERATIONS

## Discontinued Operations:

## NET INCOME before effect of acct. change

## FAS-133 transition adjustment loss (net of tax)

## INCOME FOR COMMON STOCK

## DILUTED COMMON SHARES OUT. --WEIGHTED

## INCOME FOR COMMON STOCK

## Utility

## Discontinued Operations

## Cumulative effect of accounting change

## Total

## EARNINGS PER COMMON SHARE

## Utility

## Discontinued Operations

## Cumulative effect of accounting change

## DILUTED EARNINGS PER SHARE

\* We have attempted to conform our earnings model for the company's 1Q'05 decision to sell InfrastruX and to classify this utilities service business as a discontinued operation. While management has not yet provided restated data for 3Q'05, 4Q'05, we have attempted to adjust our earnings model (even though not all rows and columns add), and use the assumption that InfrastruX will be divested by 9/30/05, even though the company says it believes the transaction will be consummated by year-end 2005. \*\*Discontinued operations include 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

D.A. Davidson & Co.

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D.A. Davidson & Co. expects to receive, or intends to seek, compensation for investment banking services from this company in the next three months.

D.A. Davidson & Co. is a full service investment firm that provides both brokerage and investment banking services. James L. Bellessa, Jr., CFA, the research analyst principally responsible for the preparation of this report, will receive compensation that is based upon (among other factors) D.A. Davidson & Co.'s investment banking revenue. However, D.A. Davidson & Co.'s analysts are not directly compensated for involvement in specific investment banking transactions.

I, James L. Bellessa, Jr., CFA, attest that (i) all the views expressed in this research report accurately reflect my personal views about the common stock of the subject company, and (ii) no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

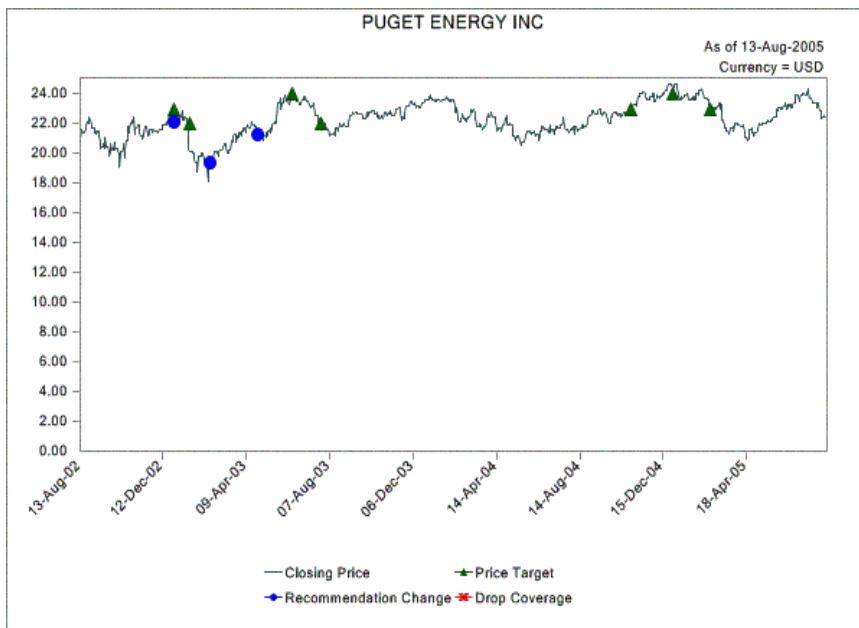
## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 6/30/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 42%	Neutral 51%	Underperform 7%
Corresponding Private Client Research Ratings and Distribution	Buy, Core/Buy 76%	Hold, Core/Hold 24%	Avoid 0%
Distribution of Combined Ratings	48%	47%	6%

### Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.

Institutional Coverage	9%	10%	9%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	7%	9%	9%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

### D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)

Buy, Neutral, Underperform

### D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)

Strong Buy, Buy, Neutral, Underperform

### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

**D.A. Davidson & Co.**

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

### **Other Disclosures**

Information contained herein has been obtained by sources we consider reliable, but is not guaranteed and we are not soliciting any action based upon it. Any opinions expressed are based on our interpretation of data available to us at the time of the original publication of the report. These opinions are subject to change at any time without notice. Investors must bear in mind that inherent in investments are the risks of fluctuating prices and the uncertainties of dividends, rates of return and yield. Investors should also remember that past performance is not necessarily an indicator of future performance and D.A. Davidson & Co. makes no guarantee, express or implied, as to future performance. Investors should note this report was prepared by D.A. Davidson & Co.'s Institutional Research Department for distribution to D.A. Davidson & Co.'s institutional investor clients and assumes a certain level of investment sophistication on the part of the recipient. Readers, who are not institutional investors or other market professionals, should seek the advice of their individual investment advisor for an explanation of this report's contents, and should always seek such advisor's advice before making any investment decisions. Further information and elaboration will be furnished upon request.

**PUGET ENERGY, INC.**

PSD – NYSE

September 1, 2005

**Rating:****NEUTRAL****Price:** (9/1/05) \$22.70**Price Targets:**

12-18 month: \$24 ↑

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

406.791.7230

jbellessa@dadco.com

FY (Dec)	2004A*	2005E**	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,198.9	\$2,480.8	13%	\$2,572.1	4%
Previous	-	NC		NC	
Price/Revenue ratio	1.0x	.9x		.9x	
<b>EPS Revised</b>	<b>\$0.55</b>	<b>\$1.44</b>	162%	<b>\$1.48</b>	3%
Previous	-	NC		NC	
Price/EPS ratio	41.2x	15.7x		15.3x	
<b>EBITDA (\$M)</b>	\$597.4	\$637.0	7%	\$704.1	11%
EV/EBITDA ratio	8.0x	7.5x		6.8x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05A**	<b>\$0.71</b>	-	\$741.7	-	\$215.9
6/30/05A**	<b>\$0.14</b>	-	\$510.1	-	\$119.3
9/30/05E**	<b>\$0.04</b>	NC	\$449.5	NC	\$104.1
12/31/05E	<b>\$0.55</b>	NC	\$779.6	NC	\$197.8

See detail of footnotes on page 2.

**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (6/30/05)	60.5%
Cash per share (6/30/05)	\$0.18
Book value per share (6/30/05)	\$16.58
Dividend (yield)	\$1.00 (4.4%)
Return on Equity (T-T-M)	5%

**Trading Data**

Shares outstanding (M)	100.3
Market Capitalization (\$M)	\$2,276
52-week range	\$20.73 - \$24.81
Average daily volume (3 mos.) (K)	288
Float	99%
Index Membership	S&P 400 MidCap

**Settlement Pact Points to Collaborative Efforts Among All Parties.****Raising Target Price. Maintaining NEUTRAL Rating.**

- Puget Sound Energy has reached a settlement agreement with all intervenors in a power cost only rate case (PCORC) that the utility filed on June 7. Essentially all components of the PCORC proposal remain intact. We expect the pact will be approved by the Washington Utilities and Transportation Commission.
- Under the agreement, electric rates would increase \$55.6 million, or 3.7%, on November 1. The rate filing was justified by the demonstrated upward pressures on the utility's power costs and the need to recover the company's \$200 million investment in the Hopkins Ridge wind power project.
- We believe the settlement agreement signals that a collaborative environment is in place for the utility to work with intervenors in the future. The pact also puts into place a procedure for updating baseline power costs on a timely basis, reducing the potential for the under-recovery of operating costs. Additionally, the \$40 million dead band will be allowed to expire on June 30, 2006, and the sharing bands under the power cost adjustment mechanism will be cut in half.
- Since our earnings model already implicitly factors in the PCORC, including \$0.03 per share for Hopkins Ridge, our EPS estimates remain unchanged. However, because the settlement agreement reduces regulatory risks and increases confidence in our 2006 estimate, we are raising our target price by one point to \$24, or 16.2x our 2006 EPS estimate. Given moderate total return prospects, including a 4.4% yield, we are maintaining a **NEUTRAL** rating.

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

\*Includes a 2004 after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

\*\*Includes 1Q'05 benefit of \$0.04/sh. for partial recovery of a previously reported regulatory disallowance related to the Tenaska gas supply regulatory asset and on-going disallowance of approximately \$0.02/sh. Includes 2Q'05 charges of \$0.02/sh for regulatory Tenaska disallowance and \$0.03/sh. for the true-up of previously reported gas costs.

\*\* Includes \$0.05 per share from discontinued operations in 2005, including (\$0.01) in 1Q'05, \$0.02 in 2Q'05, and \$0.04 in 3Q'05.

## PUGET SOUND ENERGY, INC.

## BALANCE SHEET

(\$000's; years end 12/31)

	2000	2001	2002	2003	6/30/2004	2004	6/30/2005
<b>Assets</b>							
<b>Utility Plant:</b>							
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,326,999	\$4,389,882	\$4,495,814
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,806,799	1,881,768	1,937,595
Common plant	351,051	362,670	378,844	390,622	402,869	409,677	416,119
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,386,239)	(2,452,969)	(2,522,339)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,150,428	4,228,358	4,327,189
<b>Other Property and Investments:</b>							
Total other property and investments	292,297	317,249	378,130	402,093	402,830	157,670	159,085
<b>Current Assets:</b>							
Cash	36,383	92,356	176,669	27,481	17,330	12,955	16,616
Restricted cash			18,871	2,537	1,842	1,633	1,105
Accounts receivable, net							
Less: Allowance for doubtful accounts							
Total accounts receivable	343,108	279,321	279,623	227,115	136,262	137,659	203,523
Unbilled revenues	211,784	147,008	112,115	131,798	68,084	140,391	73,295
Materials and supplies, at average cost	99,001	90,333	70,402	85,128	99,046	97,578	98,380
Purchased gas receivable	96,050	37,228			9,747	19,088	32,563
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	22,833	14,791	37,171
Taxes receivable							
Prepayments and other	11,607	11,277	11,323	12,200	17,531	8,273	18,037
Current assets of discontinued operations						110,922	116,670
Total current assets	797,933	660,838	672,744	493,852	372,675	543,290	597,360
<b>Long-Term Assets:</b>							
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	138,540	127,252	138,347
PURPA buyout costs	243,071	244,635	243,584	227,753	219,497	211,241	201,205
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	15,683	21,315	29,600
Power cost adjustment mechanism				3,605			5,518
Other	177,609	239,941	269,876	315,739	377,865	401,795	389,856
Long-term assets of discontinued operations						160,298	164,990
Total Long-term assets	628,030	680,909	690,388	698,513	751,585	921,901	929,516
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,677,518</b>	<b>\$5,851,219</b>	<b>\$6,013,150</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>							
Common stock	\$859,038	\$870	\$936	\$991	\$995	\$999	\$1,003
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,612,990	1,621,756	1,630,524
Earnings reinvested in the business	92,673	32,229	36,396	58,217	68,212	13,853	48,842
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(3,030)	(14,332)	(17,557)
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,679,167	\$1,622,276	\$1,662,812
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250	280,250	237,750
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,105,272	2,069,360	2,073,360
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	4,066,578	3,973,775	3,975,811
Minority interest in equity of a consolidated subsidiary			10,629	11,689	11,959	4,648	5,346
<b>Current Liabilities:</b>							
Accounts payable	410,619	167,426	205,619	214,357	151,910	226,478	146,537
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Purchased gas liability	0	0	83,811	11,984			
Accrued expenses:							
Taxes	103,996	70,708	62,562	77,451	63,945	81,315	97,440
Salaries and wages	17,445	14,746	11,441	12,712	13,316	13,829	14,310
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Current portion of FAS-133 unrealized losses		35,145	2,410	3,636		26,581	13,948
Tenaska disallowance reserve					13,642	3,156	0
Other	26,685	46,178	47,761	46,378	53,172	34,918	32,472
Current liabilities of discontinued operations						51,892	61,232
Total current liabilities	1,000,016	844,808	572,047	660,194	440,097	498,174	630,607
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Commitments and Contingencies	0	0	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	0	385	83
Long-term liabilities of discontinued operations						183,710	182,224
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,677,518</b>	<b>\$5,851,219</b>	<b>\$6,013,150</b>

**% of Capitalization**

Total debt and mandatory redemption preferred	64.7%	67.4%	62.3%	60.3%	59.8%	59.5%	60.5%
Preferred stock	1.4%	1.4%	1.4%	0.0%	0.0%	0.0%	0.0%
Common stock	33.9%	31.2%	36.3%	39.7%	41.3%	40.5%	41.8%
	100.0%	100.0%	100.0%	100.0%	101.1%	100.0%	102.3%

## Shares outstanding (000's)

85,904	87,023	93,643	99,074	99,487	99,868	100,286
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## Book value per share

\$16.61	\$15.66	\$16.27	\$16.71	\$16.88	\$16.24	\$16.58
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## PUGET ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)

	2003	1Q04	2Q04	3Q04	4Q04**	2004**	1Q05	2Q05	3Q05E	4Q05E	2005E	2006E
OPERATING REVENUES:												
Electric	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$ 1,423,034	\$420,090	\$345,420	\$349,126	\$443,593	\$1,558,229	\$1,608,239
Gas	634,230	275,692	119,479	89,432	284,703	769,306	321,129	162,567	99,870	335,465	919,031	961,883
Other	<u>6,043</u>	<u>527</u>	<u>553</u>	<u>2,925</u>	<u>2,531</u>	<u>6,537</u>	<u>434</u>	<u>2,127</u>	<u>500</u>	<u>500</u>	<u>3,561</u>	<u>2,000</u>
Total operating revenues	<u>2,041,016</u>	<u>668,714</u>	<u>423,123</u>	<u>415,026</u>	<u>692,012</u>	<u>2,198,877</u>	<u>741,653</u>	<u>510,114</u>	<u>449,496</u>	<u>779,558</u>	<u>2,480,821</u>	<u>2,572,122</u>
OPERATING EXPENSES:												
Energy costs:												
Purchased electricity	714,469	196,367	173,847	147,589	205,764	723,567	208,178	178,943	165,486	224,014	776,621	751,852
Purchased gas	327,132	162,407	63,703	44,574	180,618	451,302	201,744	98,142	54,969	224,693	579,548	599,734
Electric generation fuel	64,999	13,988	21,014	25,130	20,640	80,772	20,448	12,894	26,184	26,616	86,142	88,453
Residential Exchange	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(55,046)	(37,105)	(34,214)	(50,570)	(176,935)	(175,000)
Unrealized (gain)/loss on derivative instruments	106	(87)	(2,849)	1,894	516	(526)	509	(591)	0	0	(82)	0
Utility operations and maintenance	289,702	73,855	73,201	67,093	77,083	291,232	75,522	83,132	80,000	81,000	319,654	329,000
Other operations and maintenance	1,547	484	500	484	741	2,324	741	558	500	500	2,299	2,000
Depreciation and amortization	220,087	55,870	56,569	57,598	58,529	228,566	58,077	59,657	61,000	64,000	242,734	264,000
Merger and related costs/conservation amort.	33,458	8,190	4,809	4,747	4,942	22,688	5,162	5,951	5,000	5,000	21,113	22,000
Goodwill Impairment												
Taxes other than federal income taxes	194,857	64,224	42,550	42,756	59,575	208,990	69,700	50,521	48,000	71,000	239,221	252,000
Federal income taxes	<u>70,775</u>	<u>39,097</u>	<u>(5,434)</u>	<u>6,957</u>	<u>36,134</u>	<u>76,757</u>	<u>46,084</u>	<u>6,093</u>	<u>210</u>	<u>32,720</u>	<u>85,107</u>	<u>95,095</u>
Total operating expenses	1,743,292	559,972	392,548	364,808	593,868	1,911,199	631,119	458,195	407,135	678,974	2,175,423	2,229,134
OPERATING INCOME	297,724	108,742	30,575	50,218	98,144	287,678	110,534	51,919	42,361	100,584	305,398	342,988
OTHER INCOME	<u>1,587</u>	<u>68</u>	<u>1,570</u>	<u>356</u>	<u>2,392</u>	<u>4,362</u>	<u>1,164</u>	<u>1,598</u>	<u>500</u>	<u>500</u>	<u>3,762</u>	<u>2,000</u>
INCOME BEFORE INTEREST CHARGES	299,311	108,810	32,145	50,574	100,536	292,040	111,698	53,517	42,861	101,084	309,160	344,988
INTEREST CHARGES, net of AFUDC	178,488	42,043	41,842	41,104	41,574	166,539	39,582	41,527	42,500	45,000	168,609	186,000
Mandatorily redeemable securities interest	1,072	23	23	23	23	91	23	23	23	23	92	92
Preferred stock dividends of subsidiary	<u>5,151</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
INCOME FROM CONTINUING OPERATIONS	114,600	66,744	(9,720)	9,447	58,939	125,410	72,093	11,967	338	56,061	140,459	158,896
Discontinued Operations:	<u>1,766</u>	<u>(379)</u>	<u>2,940</u>	<u>1,677</u>	<u>(74,626)</u>	<u>(70,388)</u>	<u>(1,018)</u>	<u>1,928</u>	<u>4,000</u>	<u>0</u>	<u>4,910</u>	<u>0</u>
NET INCOME before effect of acct. change	116,366	66,365	(6,780)	11,124	(15,687)	55,022	71,075	13,895	4,338	56,061	145,369	158,896
FAS-133 transition adjustment loss (net of tax)	169					0						
INCOME FOR COMMON STOCK	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$71,075	\$13,895	\$4,338	\$56,061	\$145,369	\$158,896
DILUTED COMMON SHARES OUT. --WEIGHTED	95,309	99,367	99,371	100,043	99,765	99,911	100,446	100,690	100,990	101,290	100,854	107,254
INCOME FOR COMMON STOCK												
Utility	\$114,431	\$66,744	(\$9,720)	\$9,447	\$58,939	\$125,410	\$72,093	\$11,967	\$338	\$56,061	\$140,459	\$158,896
Discontinued Operations	1,766	(379)	\$2,940	\$1,677	(\$74,626)	(70,388)	(1,018)	\$1,928	\$4,000	\$0	4,910	0
Cumulative effect of accounting change	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$71,075	\$13,895	\$4,338	\$56,061	\$145,369	\$158,896
EARNINGS PER COMMON SHARE												
Utility	\$1.20	\$0.67	(\$0.10)	\$0.09	\$0.59	\$1.26	\$0.72	\$0.12	\$0.00	\$0.55	\$1.39	\$1.48
Discontinued Operations	\$0.02	(\$0.00)	\$0.03	\$0.02	(\$0.75)	(\$0.70)	(\$0.01)	\$0.02	\$0.04	\$0.00	\$0.05	\$0.00
Cumulative effect of accounting change	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>
DILUTED EARNINGS PER SHARE	\$1.22	\$0.67	(\$0.07)	\$0.11	(\$0.16)	\$0.55	\$0.71	\$0.14	\$0.04	\$0.55	\$1.44	\$1.48

\* We have attempted to conform our earnings model for the company's 1Q'05 decision to sell InfrastruX and to classify this utilities service business as a discontinued operation. While management has not yet provided restated data for 3Q'05, 4Q'05, we have attempted to adjust our earnings model (even though not all rows and columns add), and use the assumption that InfrastruX will be divested by 9/30/05, even though the company says it believes the transaction will be consummated by year-end 2005. \*\*Discontinued operations include 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

D.A. Davidson & Co.

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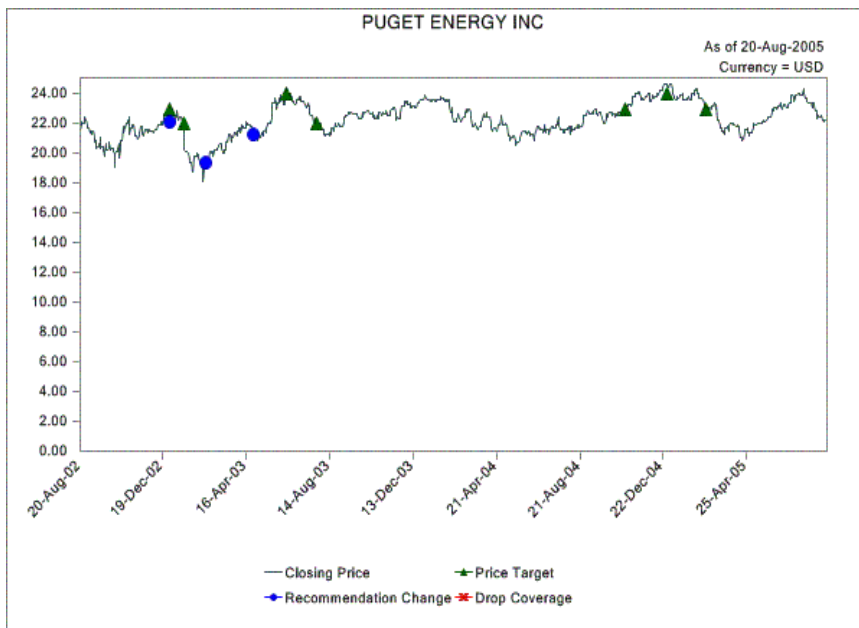
## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 8/31/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 43%	Neutral 49%	Underperform 8%
Corresponding Private Client Research Ratings and Distribution	Outperform 88%	Market Perform 12%	Underperform 0%
Distribution of Combined Ratings	51%	43%	6%

### Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.

Institutional Coverage	9%	10%	8%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	6%	10%	8%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

### D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)

Buy, Neutral, Underperform

### D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)

Strong Buy, Buy, Neutral, Underperform

### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00



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# Puget Energy

## Reaches Power Cost Only Rate Case Settlement

- Puget Energy announced yesterday that it has reached a settlement with the parties involved in its pending Power Cost Only Rate Case. The settlement appears to grant the company everything it requested, which is in line with our expectations, so we are maintaining our estimates and Neutral rating.
- We believe the potential resolution of the pending Power Cost Only Rate Case is favorable and consistent with the resolution of Puget's previous Power Cost Only Rate Case filing for its Fredrickson plant acquisition. We believe the favorable treatment of the Power Cost Only Rate Cases supports Puget's plans to invest heavily in generation over the next several years because it allows the company to quickly incorporate new assets in rates. However, the company continues to suffer from a regulatory lag as it invests in infrastructure build out at its core utility.

**Neutral**

**\$22.77**

31 August 2005

**Electric Utilities**

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**Puget Energy (PSD;PSD US)**

	2004A	2005E	2006E
EPS (\$)			
Q1 (Mar)	0.67	0.70A	
Q2 (Jun)	0.16	0.15A	
Q3 (Sep)	0.11		
Q4 (Dec)	0.61		
FY	1.60	1.40	1.55
P/E FY	14.6	16.7	15.1

Source: Company data, Reuters, JPMorgan estimates.

**Company Data**

Price (\$)	22.77
Date Of Price	31 August 05
52-week Range	20.73 - 24.81
Mkt Cap (\$ mn)	2,274.47
Fiscal Year End	Dec
Shares O/S (mn)	100
Div. Yield	4.3%

**J.P. Morgan Securities Inc.**

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## Valuation and Rating Analysis

We are maintaining our Neutral rating as Puget Energy appears to continue to struggle with regulatory lag and other factors that are preventing its core utility EPS power from emerging. We expected Puget to offer investors an attractive EPS growth profile, aided in part by a constructive regulatory outcome of the company's recent electric rate case. We believe the recent electric rate case was resolved constructively; however, the company appears to be continuing to struggle to realize the full potential of its earnings power as established in its recent rate case. Longer-term, we believe Puget still has the potential to offer investors an attractive EPS growth profile; however, it appears that the company's struggle to earn its allowed ROE will prevent the potential EPS growth from investing in its utility from emerging for at least the next several quarters. We expect the company's above-average dividend to support the shares, and the shares are trading just below the group average multiple of 15.8x 2006E EPS. Furthermore, if the company is able to address some of the issues masking its core utility earnings power, the shares appear attractively valued. For example, if the company is able to address \$0.15 of regulatory lag it is currently suffering by 2006, we estimate that the company could earn about \$1.70 in 2006, which would imply that the stock is trading at about 13.4x 2006E EPS, a significant discount to the group average 2006 multiple, especially given the company's above average yield. We believe this profile could ultimately prove attractive, but we expect the stock to trade inline with the group for the next several quarters because we do not believe visibility on potential EPS improvement will emerge over that time frame.

## Risks to Our Rating

Our Neutral rating on Puget shares is based on what we expect to be EPS dampened by regulatory lag and other factors for at least the next several quarters. This results in the company underearning its allowed ROE. If Puget continues to suffer from additional underearning pressure, or inability to add its planned utility investment to rate base, we would expect EPS, and thus the shares, to suffer. On the other hand, as we discussed above, if Puget is able to address its regulatory lag, we believe the shares appear attractive on a relative valuation. As we also discussed above, we expect visibility on this issue to take several quarters to emerge. If Puget is able to address its lag sooner rather than later, investors could get earlier visibility on higher EPS in 2006 and the shares could outperform.

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North America Equity Research  
 01 September 2005

## Companies Recommended in This Report

Puget Energy (PSD/\$22.77/Neutral)

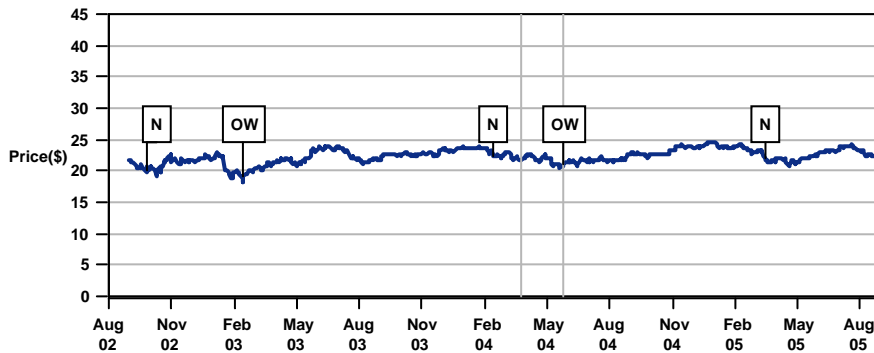
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Puget Energy (PSD) Price Chart



Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.  
 Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.  
 JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.  
 Ratings prior to Sept. 25, 2002: B = Buy, LTB = Long-Term Buy, MP = Market Performer, MU = Market Underperformer.

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Prior to September 25, 2002, our rating system was: Buy — we expect the stock to outperform the market by a minimum of 5% within an investment horizon of one year; Long-Term Buy — we believe the stock will outperform the market over the long run, but we lack the visibility of a catalyst for outperformance within a one-year investment horizon; Market Performer — the stock is expected to perform in line with the market; Market Underperformer — we expect the stock to underperform the market by a minimum of 5% within an investment horizon of one year.

Coverage Universe: **Andrew Smith:** American Electric Power (AEP), CMS Energy Corp (CMS), Calpine Corp. (CPN), Consolidated Edison (ED), Constellation Energy Group (CEG), Dominion Resources (D), Duke Energy (DUK), Entergy

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North America Equity Research  
 01 September 2005

Corp. (ETR), Exelon Corp. (EXC), FPL Group Inc. (FPL), NRG Energy (NRG), Puget Energy (PSD), Reliant Energy, Inc (RRI), Southern Company (SO), TXU Corp. (TXU), Wisconsin Energy Corp (WEC)

**JPMorgan Equity Research Ratings Distribution, as of June 30, 2005**

	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	40%	42%	18%
IB clients*	47%	46%	39%
JPMSI Equity Research Coverage	34%	49%	17%
IB clients*	66%	57%	47%

\*Percentage of investment banking clients in each rating category.

For purposes only of NASD/NYSE ratings distribution rules, our Overweight rating falls into a buy rating category, our Neutral rating falls into a hold rating category, and our Underweight rating falls into a sell rating category.

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North America Equity Research  
01 September 2005

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**North America Equity Research**  
01 September 2005

□  
Exhibit No. \_\_\_(BAV-5)  
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**PUGET ENERGY, INC.**

PSD – NYSE

September 8, 2005

**Rating:****NEUTRAL****Price:** (9/7/05) \$23.34**Price Targets:**

12-18 month: \$24

5-year: \$30

**Industry:**

Utilities

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**Key Takeaways of Investors' Presentation.**

Puget Energy's CFO, Bert Valdman, made an investors' presentation in New York City on September 7 that was webcast. The key takeaways are:

- 1) Due to solid customer growth and expiring contracts, the utility is seeking to fill an energy gap of 1,500 megawatts (MW) between 2004 and 2015.
- 2) Some 177 average megawatts (MWa) of the gap will be filled by the end of 2005 with last year's acquisition of the 50% interest (125-MW) in the Fredrickson I generating facility and the this year's completion of the 52-MW Hopkins Ridge wind power project.
- 3) In 4Q'05, the utility expects to issue an all-source request for proposals (RFP) to identify new opportunities to fill the gap under the company's least cost plan.
- 4) As a condition of the recently filed settlement agreement of the company's current power cost only rate case (PCORC), Puget expects to file a general rate case in February 2006. Included in the application will likely be requests to: a) rate base the 77-MW Wild Horse wind project, which is expected to be built in 2006; b) update baseline power costs in rates; and c) implement a new power cost adjustment mechanism to replace the present energy recovery mechanism's \$40 million deadband.
- 5) Management is forecasting that capital expenditures will be in the vicinity of \$580 million this year and \$750 million next year, including \$200 million for Hopkins Ridge and an estimated \$300-\$350 million for Wild Horse.
- 6) These capital requirements will need to be satisfied in part by an equity offering. Management stressed it has a "tremendous amount of flexibility" as to when it would raise the required equity, and "there is absolutely no hurry," due to adequate liquidity for the present period. (While our earnings model assumes a year-end 2005 offering of 5.2 million shares, raising approximately \$120 million, we acknowledge the offering will not come until management has at least the initial results from the RFP, indicating the opportunities and timing of possible resource acquisitions.)
- 7) Management is working with the Staff of the Washington Utilities and Transportation Commission (WUTC) to conceptually develop an energy delivery infrastructure tracker that would be proposed to the WUTC to allow the company to recapture some of the "lost depreciation" it faces due to regulatory lag. The company estimates it experiences an annual EPS drag of approximately \$0.10 per share because capital expenditures, incurred for other than new facilities, are not recovered on a timely basis.

Following the well-developed investors' presentation, we continue to maintain our EPS estimates for 2005 and 2006, target price of \$24, and **NEUTRAL** rating.

**RESEARCH NOTE**

Please refer to pages 2-3 of this report for detailed disclosure and certification information.



D.A. Davidson & Co.

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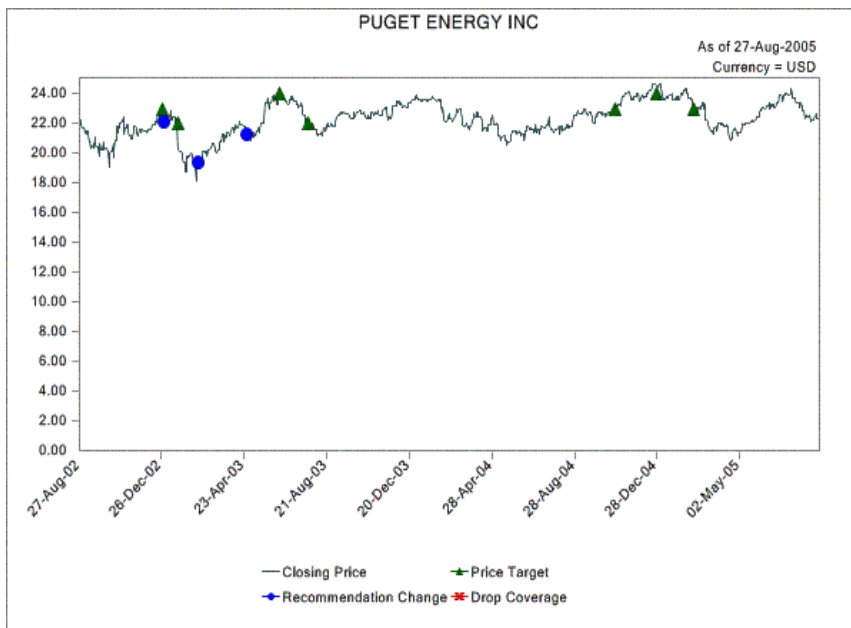
## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 8/31/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 43%	Neutral 49%	Underperform 8%
Corresponding Private Client Research Ratings and Distribution	Outperform 88%	Market Perform 12%	Underperform 0%
Distribution of Combined Ratings	51%	43%	6%

### Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.

Institutional Coverage	9%	10%	8%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	6%	10%	8%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

### D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)

Buy, Neutral, Underperform

### D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)

Strong Buy, Buy, Neutral, Underperform

### PUGET ENERGY INC

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	22-Feb-2005	22.88	23.00
14-Feb-2003	19.44	BUY	27-Dec-2004	24.62	24.00
26-Dec-2002	22.10	NEUTRAL	25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

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September 19, 2005

Stock Rating  
**Underweight**

Industry View  
**Cautious**

## Puget Energy

### Downgrade on “Regulatory Lag”: Regulator Resistance to Recovering Higher Costs

#### What's Changed

Rating **Equal-weight to Underweight**

**Conclusion:** We are downgrading PSD due to ongoing regulatory uncertainty and equity issuance needs in the face of higher spending for both fuel and operating expenses. PSD currently trades at 15.9x our 2006 estimate, which we believe to be a premium multiple for a utility in a tough regulatory environment. We expect moderate growth to come from capacity additions over time, but ongoing share issuance and constant delays in regulatory relief create a significant amount of uncertainty.

**Regulators may try to offset higher fuel pass-through costs** by limiting recovery of PSD's growing T&D spend. PSD currently has about \$0.15 of operating expense “regulatory lag” — that is, regulators typically wait two years to allow recovery of incremental spending that is already on the income statement. This situation may worsen as PSD spends approximately \$130 million more in cap ex annually versus 2003. PSD currently has a fuel-cost recovery mechanism which limits fuel under-recovery; however, regulators may not want see rates rise due to both power costs and investment. With much higher gas prices, the total implied rate hike keeps rising and we are concerned the return on equity could fall earlier.

**Implications:** We remain more positive on utilities with constructive, forward-looking regulation and unregulated baseload generation. Until we see significant change in PSD's regulatory outlook, we believe PSD will have significant difficulty improving its actual ROE of about 8.5%. Its 4.2% dividend yield provides some support for the stock, but we believe other utilities, including AEE and DTE, have better regulatory environments with comparable yields.

#### Key Ratios and Statistics

Reuters: PSD.N Bloomberg: PDS US

United States of America / Electric Utilities

Price target	NA
Shr price, close (Sep 16, 2005)	\$23.58
Mkt cap, curr (mm)	\$2,366
52-Week Range	\$24.81-20.73

	Dec 2004	Dec 2005e	Dec 2006e	Dec 2007e
<b>Year Ending</b>				
<b>ModelWare EPS (\$)</b>	1.13	1.37	1.48	1.52
<b>Prior ModelWare EPS (\$)</b>	-	-	-	-
<b>P/E</b>	21.9	17.3	15.9	15.6
Cons EPS (\$)	1.55	1.38	1.50	-
Div yld (%)	4.0	4.2	4.2	4.2

e = Morgan Stanley Research estimates  
Please see explanation of Morgan Stanley ModelWare later in this note.

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**Please see analyst certification and other important disclosures starting on page 4.**

## Investment Case

### Summary & Conclusions

#### Regulatory lag likely to grow with increased spending

PSD's T&D spending has increased from \$270 million in 2004 to an estimated \$400 million in 2006. Through 2006, PSD will only earn a return based on the lower levels of spending. For 2005, PSD has about \$0.05 of unrecovered O&M and \$0.10 of unrecovered D&A.

PSD is working on ways to overcome the \$0.15 of regulatory lag. However, we are concerned that regulators will not want to raise rates sufficiently to allow PSD to earn its theoretical 10.3% ROE until gas and power prices move down significantly. We continue to forecast high wholesale power prices for the next several years and so we do not believe that PSD will overcome that lag in the near term.

Exhibit 1

#### PSD Regulatory Lag

	2005
<b>Rate Base</b>	<b>\$3.7 Bln</b>
<b>Allowed ROE</b>	<b>10.3%</b>
<b>Theoretical EPS</b>	<b>\$1.59</b>
-D&A Lag	\$0.10
-O&M Lag	\$0.05
-Fuel Disallowance	\$0.07
<b>2005 EPS</b>	<b>\$1.37</b>
<b>Earned ROE</b>	<b>8.4%</b>
	<b>2006</b>
-Additional D&A *	\$0.03
-Additional O&M	\$0.05
+New Capacity, net equity issuance	\$0.04
+ Cust. Growth & Other	\$0.15
<b>2006 EPS</b>	<b>\$1.48</b>
<b>Earned ROE</b>	<b>8.7%</b>

\* This is based on incremental Cap Ex compared to 2003 levels.  
Source: Company data, Morgan Stanley Research

#### Next rate case filing is likely by Feb 2006

We expect the next general rate case filing to occur by February, 2006 with new rates in effect by early 2007. This should allow PSD to catch up on some unrecovered investments from 2004 and 2005. 2007 may still have lagged recovery based on 2006 and 2007 costs. The rate request is also likely to include a new power cost-sharing mechanism. The current Power Cost Adjustment (PCA) cap expires at the end of 2007 and has largely insulated PSD from recent high

power costs. A new plan may cause PSD to absorb a new round of excess power costs. Ultimately, PSD has ongoing needs for rate cases due to higher spending on fuel and operating expenses. This adds another level of uncertainty for the company.

#### Equity issuance ongoing for capacity additions

PSD is expected to raise about \$86 million in equity in late 2005 and \$150 million in late 2006 for new wind projects. While the projects have regulatory approval, the share issuance limits EPS growth and creates some overhang. Longer term, PSD is likely to issue \$100–200 million of equity annually as it continues to spend on new capacity.

#### Improved regulatory environment is chief risk of our Underweight

We do not expect PSD's regulatory environment to improve so long as fuel and purchased power costs remain high. Longer term, PSD may work out various rate structures to eliminate its regulatory lag. More forward-looking rate cases may also limit PSD's need to issue equity as it adds generating capacity.

Due to PSD's 4.2% dividend yield, a decline of interest rates also may make the stock more attractive to investors.



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### Company Description

Puget Sound Energy is a combination electric/gas utility serving the western portion of Washington state. The company delivers electricity, natural gas, and energy solutions to more than 1.2 million customers in Washington State.

### Industry View: Cautious

Historical tendency of the electrics is to underperform in a rising interest rate environment. Relative P/E is near the top of 15-year range, which may be difficult to sustain given our view of rising capex and declining margins for many utilities over the next several years.

### GICS Sector: Utilities

Strategist's Recommended Weight: 3.0%  
S&P 500 Weight: 3.5%

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Stock Rating Category	Coverage Universe		Investment Banking Clients (IBC)		
	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight/Buy	689	35%	265	40%	38%
Equal-weight/Hold	902	46%	312	47%	35%
Underweight/Sell	379	19%	93	14%	25%
<b>Total</b>	<b>1,970</b>		<b>670</b>		

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More volatile (V). We estimate that this stock has more than a 25% chance of a price move (up or down) of more than 25% in a month, based on a quantitative assessment of historical data, or in the analyst's view, it is likely to become materially more volatile over the next 1-12 months compared with the past three years. Stocks with less than one year of trading history are automatically rated as more volatile (unless otherwise noted). We note that securities that we do not currently consider "more volatile" can still perform in that manner.

Unless otherwise specified, the time frame for price targets included in this report is 12 to 18 months.

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September 19, 2005  
Puget Energy

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**Industry Coverage: Electric Utilities**

Company (Ticker)	Rating (as of)	Price (09/16/2005)
<b>Kit Konolige</b>		
Alliant Energy Corp. (LNT.N)	U (10/28/2002)	\$30.12
Ameren Corporation (AEE.N)	E (10/10/2002)	\$56.29
American Electric Power (AEP.N)	U (01/21/2005)	\$38.89
Calpine Corp. (CPN.N)	E-V (03/18/2002)	\$3.20
Cinergy (CIN.N)	E (10/28/2002)	\$44.39
CMS Energy (CMS.N)	U (01/17/2003)	\$16.58
Consolidated Edison Inc (ED.N)	E (11/05/2002)	\$49.24
DPL Inc. (DPL.N)	E (03/18/2002)	\$27.51
DTE Energy (DTE.N)	E (06/02/2005)	\$46.25
Edison International (EIX.N)	O (01/04/2005)	\$46.75
Energy East (EAS.N)	E (10/07/2002)	\$26.26
Entergy Corp. (ETR.N)	O (03/18/2002)	\$74.77
Exelon Corp. (EXC.N)	NA (04/20/2005)	\$56.92
FirstEnergy (FE.N)	O (06/02/2005)	\$52.67
FPL Group (FPL.N)	E (09/10/2002)	\$46.00
Great Plains Energy (GXP.N)	U (10/20/2004)	\$30.94
IDACORP, Inc (IDA.N)	E (08/01/2005)	\$31.30
ITC Holdings Corp. (ITC.N)	O-V (09/06/2005)	\$29.80
Northeast Utilities (NU.N)	E (11/25/2003)	\$19.89
Pepco Holdings, Inc. (POM.N)	E (03/18/2002)	\$22.89
PG&E Corp. (PCG.N)	O-V (06/16/2003)	\$38.64
Pinnacle West (PNW.N)	E (03/18/2002)	\$45.68
PPL Corp. (PPL.N)	E (12/03/2004)	\$32.36
Progress Energy Inc. (PGN.N)	E (07/01/2003)	\$44.49
PS Enterprise Group (PEG.N)	NA (12/20/2004)	\$67.70
Puget Energy (PSD.N)	Underweight (09/19/2005)	\$23.58
SCANA Corporation (SCG.N)	E (10/10/2002)	\$43.32
Southern Company (SO.N)	E (03/18/2002)	\$36.16
TECO Energy (TE.N)	E-V (07/08/2004)	\$18.16
Xcel Energy (XEL.N)	E (12/15/2003)	\$19.82
<b>Scott Soler</b>		
Constellation Energy (CEG.N)	E (03/18/2002)	\$60.95
Sempra Energy (SRE.N)	E (09/13/2004)	\$46.76
TXU Corp. (TXU.N)	E-V (08/04/2005)	\$106.40

Stock Ratings are subject to change. Please see latest research for each company.

**PUGET ENERGY, INC.**

PSD – NYSE

October 27, 2005

**Rating:****NEUTRAL****Price:** (10/27/05) \$20.83**Price Targets:**

12-18 month: \$24

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

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**Company Pre-Releases 3Q'05 and Announces Large Share Offering.**

Puget Energy pre-released third quarter results of \$0.06 per share, which exceeds our estimate for the seasonally low summer quarter, and maintained 2005 and 2006 EPS guidance.

The company also announced a 15 million share offering of common stock through a sole underwriter. No sales price to the underwriter was provided, and will not be until a filing of an addendum to the offering prospectus is made on November 1. As would be expected to clear the market of the additional supply of stock, initial trading after the share offering announcement has taken the share price to as low as \$20.50.

Net income from continuing operations for 3Q'05 fell to \$5.9 million, or \$0.06 per share, from \$11.1 million, or \$0.11 cents per share for the same quarter a year earlier. Puget also said utility net income in the quarter dropped to \$6.2 million from \$9.6 million a year ago.

We have been forecasting 3Q'05 net income from continuing operations of \$0.3 million, or \$0.00 per share, and total income of \$4.4 million, or \$0.04 per share, which also coincided with the consensus estimate of five analysts.

Management also affirmed its forecast for 2005 earnings per share from continuing operations of \$1.30-\$1.40, and its 2006 forecast of \$1.40-\$1.55.

We have been carrying a 2005 EPS estimate of \$1.44, or \$1.39 from continuing operations if an InfrastruX contribution of \$0.05 is excluded. Our 2006 estimate has been \$1.48 and assumed a January 2006 stock offering of 5.2 million shares.

Puget Energy said proceeds from the stock sale will be used by the utility business to reduce short-term debt incurred to fund its plant and equipment construction program, which prominently includes approximately \$580 million for the Hopkins Ridge and Wild Horse wind power projects. Nothing was said about the divestiture of InfrastruX, which management previously said would be a likely 2005 event.

We will rework our earnings model for this new information and will publish an update once the company reports full 3Q'05 financial results on November 1, 2005. Tentatively, we view the strengthening of the balance sheet from the share offering as a positive, assuring financing for the company's aggressive capital expenditure program. We believe the share offering moves the equity ratio from approximately 40% on September 30, 2005 to about 43%, which matches the target level set by regulators in a recent rate case.

We are also impressed by management's maintenance of the 2006 guidance range in the wake of a significantly larger share offering than we were expecting. If our earnings forecast is maintained, after we factor in the dilution of the share offering, we expect the shares will trade in the vicinity of \$21-\$22, or 14.0x-15.0x the mid-point of the 2006 guidance range, once the market absorbs the approximate 15% increase in outstanding shares. In the interim period, our 12-18 month target price remains \$24.

**RESEARCH NOTE**

Please refer to pages 2-3 of this report for detailed disclosure and certification information.

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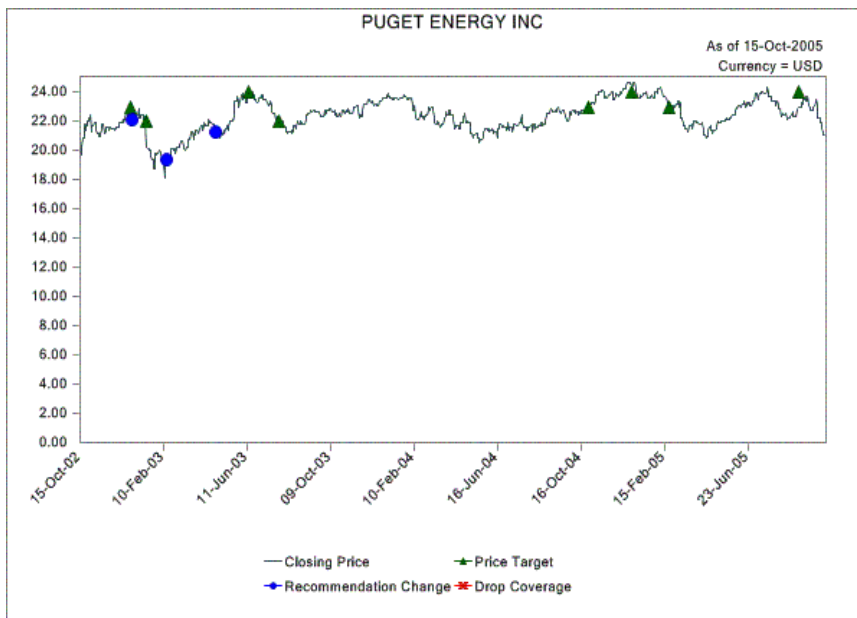
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## Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 9/30/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 42%	Neutral 48%	Underperform 10%
Corresponding Private Client Research Ratings and Distribution	Outperform 85%	Market Perform 15%	Underperform 0%
Distribution of Combined Ratings	49%	43%	8%

Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.	Buy	Hold	Sell
Institutional Coverage	6%	9%	13%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	4%	8%	13%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
Strong Buy, Buy, Neutral, Underperform

PUGET ENERGY INC					
Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	01-Sep-2005	22.90	24.00
14-Feb-2003	19.44	BUY	22-Feb-2005	22.88	23.00
26-Dec-2002	22.10	NEUTRAL	27-Dec-2004	24.62	24.00
			25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

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# Puget Energy

## Sizeable Equity Offering Dilutes EPS, Adj. Ests.

- We are maintaining our Neutral rating on PSD, but cutting 2006 EPS estimates to \$1.40 from \$1.55 on the basis of Puget's equity offering of 15 million shares of common stock. We expect PSD's earnings to be at the lower end of the company's guidance range, but we also expect the shares to have yield support near their current trading level. Accordingly, we expect the shares to perform about inline with their peer group.
- PSD announced after the market close on 10/26 that it is offering 15 million shares of common stock in an overnight placement. and has an option to place an additional 1.7 million shares. As previously disclosed, PSD plans to use the proceeds to fund its capital spending program at its utility, Puget Sound Energy. While we were not surprised by Puget's equity offer given its infrastructure investment plans, we are surprised by the size of the offer because the company appears to be selling about \$60-100 million more equity than it needs.
- Furthermore, we believe that Puget's equity offer and the corresponding EPS dilution highlights the regulatory lag problems that the company has been suffering. The company previously indicated that it expects about a negative \$0.11 per share impact from regulatory lag. In the context of the equity offer, based on Puget's allowed rate base from its recent general rate case, if we incorporate its recent equity offer as well as its planned \$580 million rate base addition from its wind farm investments (which it

### Puget Energy (PSD;PSD US)

	2004A	2005E	2006E (Old)	2006E (New)
EPS (\$)				
Q1 (Mar)	0.67	0.70A		
Q2 (Jun)	0.16	0.15A		
Q3 (Sep)	0.11	0.06A		
Q4 (Dec)	0.61			
FY	1.60	1.40	1.55	1.40
P/E FY	12.9	14.8	13.3	14.8

Source: Company data, Reuters, JPMorgan estimates.

**Neutral**

**\$20.70**

27 October 2005

### Electric Utilities

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### Company Data

Price (\$)	20.70
Date Of Price	27 October 05
52-week Range	20.71 - 24.81
Mkt Cap (\$ mn)	2,450.65
Fiscal Year End	Dec
Shares O/S (mn)	115
Div. Yield	4.8%

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can add to rate base through its expedited resource planning regulatory filing, the Power Cost Only Rate Case), we project that the equity layer at its utility is about 46%. This is well above the 43% equity layer that Puget is allowed to incorporate into rates. We note that if Puget is able to correct its regulatory lag problem and incorporate about \$780 million of delivery infrastructure spending (\$300 million net of D&A) into its rate making structure, its utility equity layer falls to about 43%, in line with its allowed regulatory structure, but it does not appear to us that this problem will be resolved anytime soon.

- Given the sizeable stock dilution, we are decreasing our 2006 EPS estimate to \$1.40. The stock is trading at 14.8x 2006E EPS, about inline with the group average of 14.5x. We also do not expect Puget to offer investors material earnings growth in the near-term; however, we expect its dividend yield of 4.8%, well above the group average of 4%, to likely support the stock. Accordingly, we believe Puget could be an attractive investment for investors interested in income generation, but we expect the shares to perform inline with their peers.

## EPS and Equity Layer Projections

Our EPS projections and equity layer calculations assuming only Puget's wind farm spending is incorporated into its rate base are shown in Table 1, below. As shown by our calculations, Puget's equity layer at its utility is about 46% on this basis. Table 2 incorporates not only Puget's wind farm investments, but also its planned delivery infrastructure investment net of D&A. This results in a projected equity layer of about 43%. We believe these two tables illustrate the regulatory lag Puget currently is suffering as it is not able to incorporate its full utility investment in its rates.

**Table 1: EPS and Equity Layer Projections Assuming Only Wind Farm Investments Added to Rate Base**

\$ million			
Equity Offer Stock Price	20.70		
Shares Offered (millions)	15		
Equity Offer	311		
Hopkins Wind Farm Spending	200		
Wild Horse Wind Farm Spending	380		
Total Wind Farm Spending	580		
Equity Needed to Fund Wind Expansion @ 43% Equity	249		
Projected Equity Offer	311		
Excess Equity Offer Assumed Used for Debt Paydown	61		
<b>EPS Reconciliation</b>	<b>2005E</b>	<b>2006E</b>	<b>2007E</b>
Gas Rate Base (\$ Millions)	1,068	1,068	1,068
Electric Rate Base (\$ Millions)	2,545	2,545	2,545
Additions to Rate Base - Wind Projects (\$ Millions)	0	580	580
Total Rate Base (\$ Bn)	3,612	4,192	4,192
Equity Layer	43.00%	43.00%	43.00%
Allowed ROE	10.30%	10.30%	10.30%
Shares (millions)	100	115	115
<b>Projected Utility EPS</b>	<b>1.60</b>	<b>1.61</b>	<b>1.61</b>
Less: D&A Lag	-0.10	-0.08	0.00
Less: Incremental O&M	-0.05	-0.03	0.00
Less: Additional Debt Cost @ 7% for Wind Projects		-0.13	-0.13
Plus: Debt Paydown from Excess Equity Offer @ 7%		0.02	0.02
<b>Projected Ongoing EPS</b>	<b>1.45</b>	<b>1.40</b>	<b>1.51</b>
P/E	14.3x	14.8x	13.9x
Projected ROE Excluding Tenaska Disallowance	9.3%	8.9%	9.6%
<b>PRO FORMA EQUITY LAYER CALCULATIONS</b>	<b>\$ millions</b>		
Rate Base per General Rate Case	3,612		
Wind Farm Additions to Rate Base	580		
Pro Forma Rate Base	4,192		
Equity Layer Pre Equity Offer (6/30/05 balance sheet)	1,631		
New Equity from Equity Offer	311		
Pro Forma Equity Layer	1,941		
<b>Pro Forma Equity Ratio</b>	<b>46%</b>		

Source: JPMorgan estimates, Company data.



**Table 2: Equity Layer Projections Assuming Wind Projects and Delivery Infrastructure Spending Added to Rate Base**

\$ million	
Equity Offer Stock Price	20.70
Shares Offered (millions)	15
Equity Offer	311
Hopkins Wind Farm Spending	200
Wild Horse Wind Farm Spending	380
Total Wind Farm Spending	580
Additional Rate Base Spending 2005 & 2006	780
Less: Expected D&A 2005 & 2006	480
Net Rate Base Additions	300
<b>PRO FORMA EQUITY LAYER CALCULATIONS</b>	
	<b>\$ millions</b>
Rate Base per General Rate Case	3,612
Net Additions to Rate Base (Wind Farms & Delivery Capex)	880
Pro Forma Rate Base	4,492
<b>Pro Forma Utility Equity Layer - Rate Making Basis</b>	
Equity Layer Pre Equity Offer (6/30/05 balance sheet)	1,631
New Equity from Equity Offer	311
Pro Forma Equity Layer	1,941
<b>Pro Forma Equity Ratio</b>	<b>43%</b>

Source: JPMorgan estimates, Company data.

## Valuation and Rating Analysis

We are maintaining our Neutral rating as Puget Energy appears to continue to struggle with regulatory lag and other factors that are preventing its core utility EPS power from emerging. We expected Puget to offer investors potentially modest earnings growth, if any, in 2006 given that its recent sizeable equity offer results in significant EPS dilution in 2006. Longer-term, we believe Puget may still have the potential to offer investors an attractive EPS growth profile; however, it appears that the company's struggle to earn its allowed ROE may prevent the potential EPS growth from investing in its utility from being realized for at least the next several quarters. We expect the company's above average dividend to support the shares, and the shares are trading just above the group average multiple of 14.5x 2006E EPS. Furthermore, if the company is able to address some of the issues masking its core utility earnings power, the shares appear attractively valued. For example, if the company is able to address \$0.11 of regulatory lag it is currently suffering by 2006, we estimate that the company could earn about \$1.50-1.55 in 2006, which would imply that the stock is trading at about 13.5x 2006E EPS, a discount to the group average 2006 multiple, especially given the company's above average yield. We believe this profile could ultimately prove attractive, but we expect the stock to trade inline with the group for the next several quarters because we do not believe visibility on potential EPS improvement will emerge over that time frame.

## Risks to Our Rating

Our Neutral rating on Puget shares is based on what we expect to be EPS dampened by regulatory lag and common share dilution for at least the next several quarters. This results in the company underearning its allowed ROE. If Puget continues to suffer from additional underearning pressure, or inability to add its planned utility investment to rate base, we would expect EPS, and thus the shares, to suffer. On the other hand, as we discussed above, if Puget is able to address its regulatory lag, we believe the shares appear attractive on a relative valuation. As we also discussed above, we expect visibility on this issue to take several quarters to emerge. If Puget is able to address its lag sooner rather than later, investors could get earlier visibility on higher EPS in 2006 and the shares could outperform.

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North America Equity Research  
 27 October 2005

**Companies Recommended in This Report (as of COB 27 October 2005)**

Puget Energy (PSD/\$20.70/Neutral)

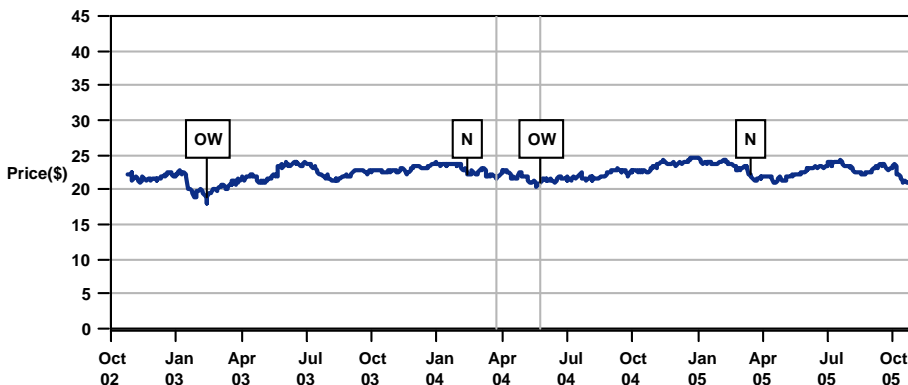
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**Puget Energy (PSD) Price Chart**



Date	Rating	Share Price (\$)	Price Target (\$)
13-Feb-03	OW	19.00	-
12-Feb-04	N	22.31	-
25-May-04	OW	21.14	-
14-Mar-05	N	22.15	-

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.  
 Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.  
 JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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North America Equity Research  
27 October 2005

#### JPMorgan Equity Research Ratings Distribution, as of September 30, 2005

	Overweight (buy)	Neutral (hold)	Underweight (sell)
JPM Global Equity Research Coverage	40%	42%	18%
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IB clients*	65%	55%	45%

\*Percentage of investment banking clients in each rating category.

For purposes only of NASD/NYSE ratings distribution rules, our Overweight rating falls into a buy rating category, our Neutral rating falls into a hold rating category, and our Underweight rating falls into a sell rating category.

**Valuation and Risks:** Company notes and reports include a discussion of valuation methods used, including methods used to determine a price target (if any), and a discussion of risks to the price target.

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North America Equity Research  
27 October 2005

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**North America Equity Research**  
27 October 2005

□  
Exhibit No. \_\_\_(BAV-5)  
Page 237 of 297

November 3, 2005

**PUGET ENERGY, INC.**

PSD – NYSE

**Rating:****NEUTRAL****Price:** (11/2/05) \$21.03**Price Targets:**

12-18 month: \$23 ↓

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

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FY (Dec)	2004A <sup>1</sup>	2005E <sup>2</sup>	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,198.9	\$2,523.4	15%	\$2,602.6	3%
Previous	-	\$2,480.8		\$2,572.1	
Price/Revenue ratio	1.0x	.9x		1.0x	
<b>EPS Revised</b>	<b>\$1.26</b>	<b>\$1.39</b>	11%	<b>\$1.43</b>	3%
Previous	-	\$1.44		\$1.48	
Price/EPS ratio	16.8x	15.1x		14.7x	
<b>EBITDA (\$M)</b>	\$597.4	\$642.1	7%	\$710.0	11%
EV/EBITDA ratio	7.8x	7.3x		6.6x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05A	<b>\$0.72</b>	-	\$741.7	-	\$215.9
6/30/05A	<b>\$0.12</b>	-	\$510.1	-	\$119.3
9/30/05A	<b>\$0.06</b>	\$0.04	\$490.4	\$449.5	\$112.0
12/31/05E	<b>\$0.48</b>	\$0.55	\$781.3	\$779.6	\$195.0

EPS now represents results from continuing operations. <sup>1,2</sup>See detail of footnotes on page 2.**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (9/30/05)	60.7%
Cash per share (9/30/05)	\$0.11
Book value per share (9/30/05)	\$16.61
Dividend (yield)	\$1.00 (4.8%)
Return on Equity (T-T-M)	5%

**Trading Data**

Shares outstanding (M)	100.5
Market Capitalization (\$M)	\$2,113
52-week range	\$20.50 - \$24.81
Average daily volume (3 mos.) (K)	331
Float	99%
Index Membership	S&P 400 MidCap

**Company Description:**

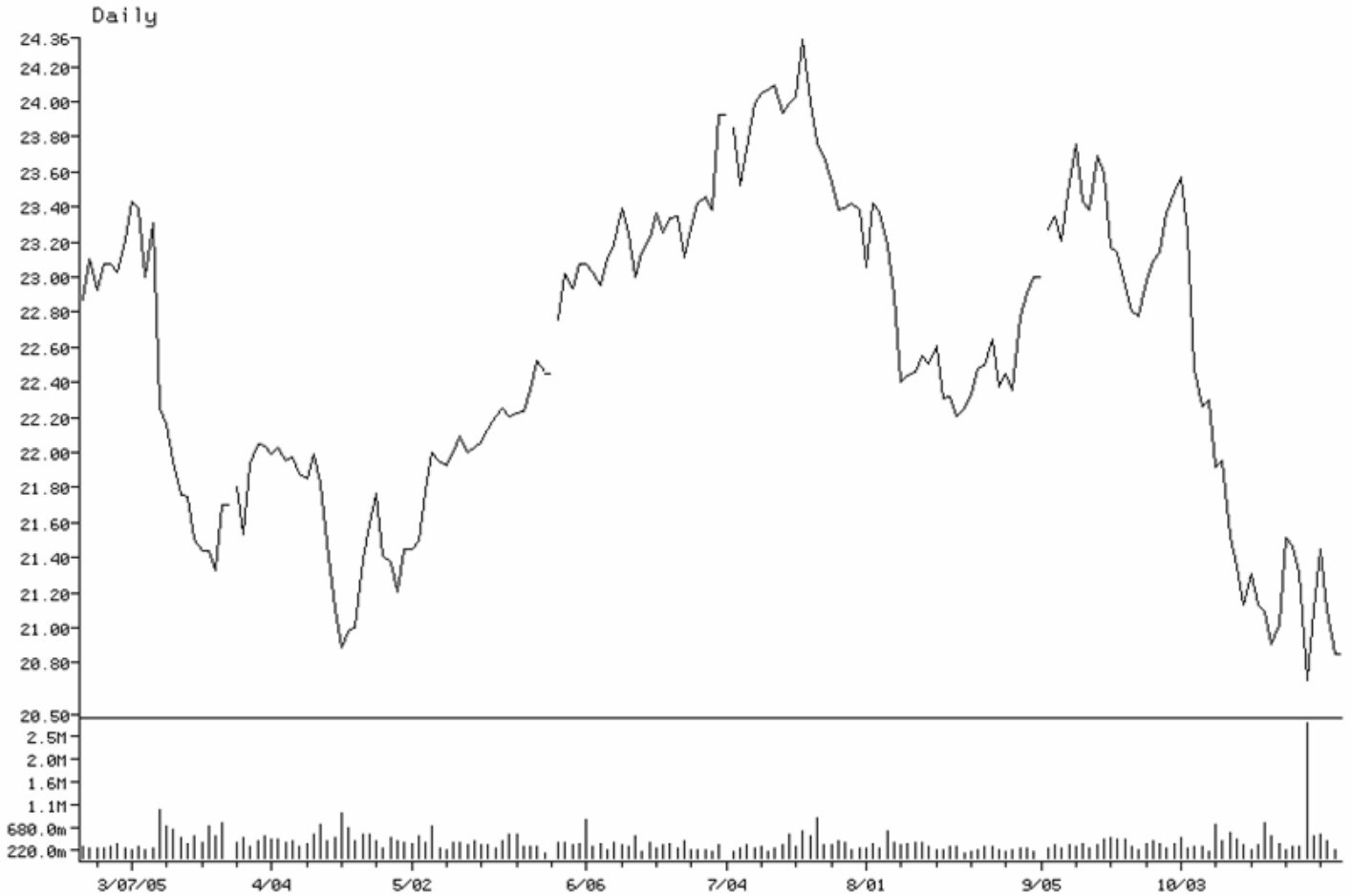
Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Trimming 2006 EPS Forecast and Target Due to Share Offering Dilution. Maintaining NEUTRAL Rating.**

- Puget Energy reported 3Q'05 net income from continuing operations of \$0.06 per diluted share, compared to \$0.09 per share, in 3Q'04. Quarterly figures matched data disclosed in the company's October 26 pre-release of results. Prior to the pre-release, we were forecast EPS of \$0.04.
- Higher utility operations and maintenance costs and plant depreciation expense during 3Q'05 offset the impact of an increase in margins from higher energy sales to electric and natural gas customers.
- Due to the dilution from a recent share offering, we have re-worked our earnings model and are reducing our 2005 EPS estimate to \$1.39 from continuing operations, from \$1.44 of consolidated earnings. Our forecast of earnings from continuing operations remains unchanged.
- Our 2006 EPS forecast is being reduced from \$1.48 to \$1.43, as a 10% higher number of shares than we were previously forecasting more than offsets an improved operating assumption.
- Based on a reduced 2006 EPS expectation, we are lowering our 12-18 month target price by a point to \$23, or 16.0x our revised 2006 EPS estimate. At the current share price, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock remains the current yield of 4.8%.

Please refer to pages 7-8 of this report for detailed disclosure and certification information.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

<sup>1</sup>2004 data includes an after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

<sup>2</sup>2005 data includes 1Q'05 benefit of \$0.04/sh. for partial recovery of a previously reported regulatory disallowance related to the Tenaska gas supply regulatory asset and on-going disallowance of approximately \$0.02/sh. Includes 2Q'05 charges of \$0.02/sh for regulatory Tenaska disallowance and \$0.03/sh. for the true-up of previously reported gas costs.

2004 and 2005 data excludes results from discontinued operations, including (\$0.70) in 2004, (\$0.01) in 1Q'05, \$0.02 in 2Q'05.



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**Operating Results Match Pre-Release**

Puget Energy reported 3Q'05 net income from continuing operations of \$5.9 million, or \$0.06 per diluted share, compared to net income of \$9.4 million, or \$0.09 per share, in 3Q'04. Quarterly figures matched data disclosed in the company's October 26 pre-release of results. Prior to the pre-release, we were forecasting EPS of \$0.04.

Now reported as discontinued operations, InfrastruX contributed \$0.00 per share to 3Q'05 earnings, compared to \$0.02 per share a year ago. The recent quarter's InfrastruX results included an \$0.08 per share charge to adjust Puget Energy's carrying value to the estimate of fair value, less cost to sell this unit. Puget is attempting to monetize its investment in InfrastruX through a sale or third party recapitalization. While the amount InfrastruX will be divested for is uncertain, Puget says the sales proceeds will be invested in the regulated utility. The timing of the InfrastruX divestiture also remains uncertain. While the transaction could still be consummated before year-end 2005, management acknowledged the sale could slip into 1Q'06. Our earnings model now uses earnings from continuing operations, so results from InfrastruX are not included in our 2005 and 2006 forecasts or historical comparisons.

**Rate Relief and Customer Growth Help Utility Results**

Quarterly electric revenues of \$375 million climbed \$52 million, or 16%, primarily due to a \$22 million increase in electric retail sales and a \$24 million increase in electric wholesale sales. The electric retail increase was aided by rate increases and higher retail customer usage. The increase in sales to other utilities and marketers was due to a 145% increase in megawatt-hour (Mwh) volumes related to excess generation available for sale on the wholesale market.

The jump in wholesale Mwh sales resulted when normal streamflows for hydro electric generation occurred instead of below normal streamflows that the company anticipated going into the quarter. The increase in MWh sold was due to differences in timing of the need for power to serve base load and actual weather conditions. These wholesale sales did not materially benefit earnings, as sales to other utilities and marketers are included in the power cost adjustment (PCA) mechanism as a reduction in determining the regulated utility's net power costs.

Retail sales rose \$22.0 million due to a 4.1% increase in electric rates that went into effect on March 4, 2005 and 1.8% customer growth. After deducting the costs of generating and purchasing electric energy from electric revenues, Puget Sound Energy had electric margins of \$150 million versus \$149 million in 3Q'04. Benefits of the rate case that helped electric margins were offset by additional recovery of power costs through the PCA, which does not increase margin.

Quarterly gas revenues of \$111 million rose \$22 million, or 24%, primarily due to higher tariffs under the current Purchased Gas Adjustment mechanism to recover higher purchased gas costs, as well as last March's 3.5% general gas rate increase and 2.9% customer growth. After deducting the costs of gas sales, to retail and transportation customers, from gas revenues, gas margins were \$49 million in 3Q'05, which were up \$4.0 million, or 13%, from 3Q'04.

Higher utility operations and maintenance costs and plant depreciation expense during 3Q'05 offset the impact of an increase in margins from higher energy sales to electric and natural gas customers.

**Share Offering Injects Capital**

On October 26, 2005, management announced an overnight common stock offering of 15,000,000 shares through a sole underwriter. The public offering price was \$20.80, with the company garnering \$309.8 million in new capital, net of offering expenses. The company granted the underwriter a 30-day option to purchase up to an additional 1,690,000 shares on the same terms and conditions if the underwriters sell more than 15,000,000 shares of common stock in this offering. Initial offering proceeds were invested in the firm's utility subsidiary, Puget Sound Energy, which used the proceeds to repay a portion of its outstanding short-term debt that has been incurred to fund capital expenditures and for general corporate

purposes. Immediately, Puget's equity ratio jumped from 39% to 46%, but by the end of the year the ratio will have retreated to about 43%, once planned capital expenditures are made.

**Maintaining 2005 EPS Forecast,  
But Trimming 2006 Projection**

Management reiterated 2005 EPS guidance of \$1.30-\$1.40. Due to the dilution from the share offering, we have re-worked our earnings model and are reducing our 2005 EPS estimate to \$1.39 from continuing operations, from \$1.44 from consolidated earnings, including InfrastruX. Our forecast of earnings from continuing operations remains unchanged.

Management continues to provide 2006 EPS guidance of \$1.40-\$1.55 per diluted share from continuing operations, assuming normal weather conditions. Our 2006 EPS forecast is being reduced from \$1.48 to \$1.43, as a higher number of shares than we were previously forecasting more than offsets an improved operating assumption.

Our revised 2006 projection of an 18% increase in consolidated net income from continuing operations is being diluted by a 15% increase in average shares outstanding, chiefly due to the October 26 stock offering of approximately 15.0 million shares to help finance capital expenditures, especially for two wind power projects. The \$190 million Hopkins Ridge wind project, with 150-megawatts (MW) of capacity, or 52 average MW, is currently being tested and should be in full operation by year-end 2005. The \$380 million Wild Horse wind project, with approximately 230-MW of capacity, or 73 average MW, should be operating by year-end 2006. The utility plans to file a power cost only rate case (PCORC) in February 2006 with the Washington Utilities and Transportation Commission (WUTC) to help recover the higher cost of power, including the costs of the Hopkins Ridge wind power project. A WUTC decision for the PCORC is expected by year-end 2006, if not settled prior to a rate proceeding.

**Maintaining Target Price and  
NEUTRAL Rating**

Based on a reduced 2006 EPS expectation, we are lowering our 12-18 month target price by a point to \$23, or 16.0x our revised 2006 EPS estimate. Over the past decade, the stock of PSD has traded at a median 15.1x multiple of year-forward earnings. At the current share price, we are maintaining our **NEUTRAL** rating. The chief attraction to the stock remains the current yield of 4.8%.

James L. Bellessa Jr., CFA  
Vice President, Senior Research Analyst  
406.791.7230

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

	2000	2001	2002	2003	2004	9/30/2005A
<b>Assets</b>						
<b>Utility Plant:</b>						
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,389,882	\$4,645,289
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,881,768	1,966,806
Common plant	351,051	362,670	378,844	390,622	409,677	436,822
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,452,969)	(2,566,492)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,228,358	4,482,425
<b>Other Property and Investments:</b>						
Total other property and investments	292,297	317,249	378,130	402,093	157,670	157,249
<b>Current Assets:</b>						
Cash	36,383	92,356	176,669	27,481	12,955	9,817
Restricted cash			18,871	2,537	1,633	1,045
Accounts receivable, net						
Less: Allowance for doubtful accounts						
Total accounts receivable	343,108	279,321	279,623	227,115	137,659	112,283
Unbilled revenues	211,784	147,008	112,115	131,798	140,391	81,265
Inventories and supplies, at average cost	99,001	90,333	70,402	85,128	97,578	129,027
Purchased gas receivable	96,050	37,228			19,088	37,508
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	14,791	203,419
Taxes receivable						
Prepayments and other	11,607	11,277	11,323	12,200	8,273	34,485
Current assets of discontinued operations					110,922	122,664
Total current assets	797,933	660,838	672,744	493,852	543,290	731,513
<b>Long-Term Assets:</b>						
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	127,252	135,194
PURPA buyout costs	243,071	244,635	243,584	227,753	211,241	196,188
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	21,315	38,956
Power cost adjustment mechanism				3,605		5,583
Other	177,609	239,941	269,876	315,739	401,795	383,662
Long-term assets of discontinued operations					160,298	161,753
Total Long-term assets	628,030	680,909	690,388	698,513	921,901	921,336
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,851,219</b>	<b>\$6,292,523</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>						
Common stock	\$859,038	\$870	\$936	\$991	\$999	\$1,005
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,621,756	1,634,600
Earnings reinvested in the business	92,673	32,229	36,396	58,217	13,853	29,679
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(14,332)	3,266
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,622,276	\$1,668,550
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250	237,750
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,069,360	2,068,360
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	3,973,775	3,976,549
Minority interest in equity of a consolidated subsidiary			10,629	11,689	4,648	6,151
<b>Current Liabilities:</b>						
Accounts payable	410,619	167,426	205,619	214,357	226,478	216,668
Short-term debt	378,316	348,577	47,295	13,893		223,871
Current maturities of long-term debt	19,000	119,523	73,206	246,829	31,000	46,000
Purchased gas liability	0	0	83,811	11,984		
Accrued expenses:						
Taxes	103,996	70,708	62,562	77,451	81,315	77,297
Salaries and wages	17,445	14,746	11,441	12,712	13,829	12,125
Interest	43,955	42,505	37,942	32,954	29,005	42,901
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	26,581	14,643
Tenaska disallowance reserve					3,156	0
Other	26,685	46,178	47,761	46,378	34,918	28,994
Current liabilities of discontinued operations					51,892	73,783
Total current liabilities	1,000,016	844,808	572,047	660,194	498,174	755,875
Deferred Income Taxes	608,185	605,315	730,675	755,235	795,291	760,382
Other Deferred Credits	132,869	196,339	267,458	340,893	395,236	620,525
Commitments and Contingencies	0	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	385	0
Long-term liabilities of discontinued operations					183,710	173,041
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,851,219</b>	<b>\$6,292,523</b>

**% of Capitalization**

Total debt and mandatory redemption preferred	64.7%	67.4%	62.3%	60.3%	59.5%	60.7%
Preferred stock	1.4%	1.4%	1.4%	0.0%	0.0%	0.0%
Common stock	<u>33.9%</u>	<u>31.2%</u>	<u>36.3%</u>	<u>39.7%</u>	<u>40.5%</u>	<u>39.3%</u>
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Shares outstanding (000's)	85,904	87,023	93,643	99,074	99,868	100,460
Book value per share	\$16.61	\$15.66	\$16.27	\$16.71	\$16.24	\$16.61
Book value per share for the utility			\$15.23	\$15.70	\$15.95	\$16.29

## PUGET ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)

	2003	1Q04	2Q04	3Q04	4Q04**	2004**	1Q05	2Q05	3Q05	4Q05E	2005E	2006E
OPERATING REVENUES:												
Electric	\$1,400,743	\$392,495	\$303,091	\$322,669	\$404,778	\$1,423,034	\$420,090	\$345,420	\$375,035	\$445,330	\$1,585,875	\$1,620,739
Gas	634,230	275,692	119,479	89,432	284,703	769,306	321,129	162,567	111,042	335,465	930,203	974,363
Other	6,043	527	553	2,925	2,531	6,537	434	2,127	4,306	500	7,367	7,500
Total operating revenues	2,041,016	668,714	423,123	415,026	692,012	2,198,877	741,653	510,114	490,383	781,295	2,523,445	2,602,602
OPERATING EXPENSES:												
Energy costs:												
Purchased electricity	714,469	196,367	173,847	147,589	205,764	723,567	208,178	178,943	200,861	235,134	823,116	810,370
Purchased gas	327,132	162,407	63,703	44,574	180,618	451,302	201,744	98,142	59,151	221,713	580,750	590,159
Electric generation fuel	64,999	13,988	21,014	25,130	20,640	80,772	20,448	12,894	21,058	26,720	81,120	81,037
Residential Exchange	(173,840)	(54,423)	(35,362)	(34,014)	(50,674)	(174,473)	(55,046)	(37,105)	(34,525)	(50,768)	(177,444)	(177,000)
Unrealized (gain)/loss on derivative instruments	106	(87)	(2,849)	1,894	516	(526)	509	(591)	477	0	395	0
Utility operations and maintenance	289,702	73,855	73,201	67,093	77,083	291,232	75,522	83,132	81,645	82,000	322,299	329,000
Other operations and maintenance	1,547	484	500	529	741	2,324	741	558	745	500	2,544	2,000
Depreciation and amortization	220,087	55,870	56,569	57,598	58,529	228,566	58,077	59,657	60,550	64,000	242,284	264,000
Merger and related costs/conservation amort.	33,458	8,190	4,809	4,747	4,942	22,688	5,162	5,951	5,633	5,500	22,246	22,000
Goodwill Impairment												
Taxes other than federal income taxes	194,857	64,224	42,550	42,710	59,575	208,990	69,700	50,521	44,784	66,000	231,005	240,000
Federal income taxes	70,775	39,097	(5,434)	6,958	36,134	76,757	46,084	6,093	2,476	32,793	87,446	101,209
Total operating expenses	1,743,292	559,972	392,548	364,808	593,868	1,911,199	631,119	458,195	442,855	683,593	2,215,762	2,262,774
OPERATING INCOME	297,724	108,742	30,575	50,218	98,144	287,678	110,534	51,919	47,528	97,703	307,684	339,828
OTHER INCOME	1,587	68	1,570	356	2,392	4,362	1,164	1,598	1,422	500	4,684	5,000
INCOME BEFORE INTEREST CHARGES	299,311	108,810	32,145	50,574	100,536	292,040	111,698	53,517	48,950	98,203	312,368	344,828
INTEREST CHARGES, net of AFUDC	178,488	42,043	41,842	41,104	41,574	166,539	39,582	41,527	43,015	44,000	168,124	174,000
Mandatorily redeemable securities interest	1,072	23	23	23	23	91	23	23	23	23	92	92
Preferred stock dividends of subsidiary	5,151	0	0	0	0	0	0	0	0	0	0	0
INCOME FROM CONTINUING OPERATIONS	114,600	66,744	(9,720)	9,447	58,939	125,410	72,093	11,967	5,912	54,180	144,152	170,736
Discontinued Operations:	1,766	(379)	2,940	1,677	(74,626)	(70,388)	(1,018)	1,928	(1)	0	909	0
NET INCOME before effect of acct. change	116,366	66,365	(6,780)	11,124	(15,687)	55,022	71,075	13,895	5,911	54,180	145,061	170,736
FAS-133 transition adjustment loss (net of tax)	169					0						
INCOME FOR COMMON STOCK	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$71,075	\$13,895	\$5,911	\$54,180	\$145,061	\$170,736
DILUTED COMMON SHARES OUT. --WEIGHTED	95,309	99,367	99,371	100,043	99,765	99,911	100,446	100,690	100,964	111,831	103,483	119,164
INCOME FOR COMMON STOCK												
Utility	\$114,431	\$66,744	(\$9,720)	\$9,447	\$58,939	\$125,410	\$72,093	\$11,967	\$5,912	\$54,180	\$144,152	\$170,736
Discontinued Operations	1,766	(379)	2,940	1,677	(74,626)	(70,388)	(1,018)	1,928	(\$1)	0	909	0
Cumulative effect of accounting change	0	0	0	0	0	0	0	0	0	0	0	0
Total	\$116,197	\$66,365	(\$6,780)	\$11,124	(\$15,687)	\$55,022	\$71,075	\$13,895	\$5,911	\$54,180	\$145,061	\$170,736
EARNINGS PER COMMON SHARE												
Utility	\$1.20	\$0.67	(\$0.10)	\$0.09	\$0.59	\$1.26	\$0.72	\$0.12	\$0.06	\$0.48	\$1.39	\$1.43
Discontinued Operations	\$0.02	(\$0.00)	\$0.03	\$0.02	(\$0.75)	(\$0.70)	(\$0.01)	\$0.02	(\$0.00)	\$0.00	\$0.01	\$0.00
Cumulative effect of accounting change	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
DILUTED EARNINGS PER SHARE	\$1.22	\$0.67	(\$0.07)	\$0.11	(\$0.16)	\$0.55	\$0.71	\$0.14	\$0.06	\$0.48	\$1.40	\$1.43

\* We have attempted to conform our earnings model for the company's 1Q'05 decision to sell InfrastruX and to classify this utilities service business as a discontinued operation. While management has not yet provided restated data for 4Q'05, we have attempted to adjust our earnings model (even though not all rows and columns add), and use the assumption that InfrastruX will be divested by 12/30/05. \*\*Discontinued operations include 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

D.A. Davidson & Co.

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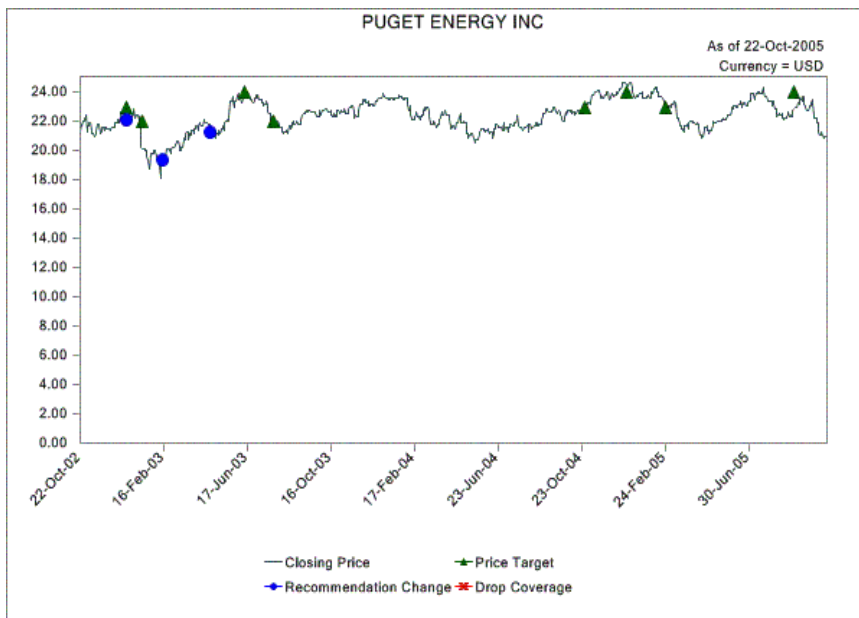
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D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 9/30/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 42%	Neutral 48%	Underperform 10%
Corresponding Private Client Research Ratings and Distribution	Outperform 85%	Market Perform 15%	Underperform 0%
Distribution of Combined Ratings	49%	43%	8%

Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.	Buy	Hold	Sell
Institutional Coverage	6%	9%	13%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	4%	8%	13%



D.A. Davidson & Co. has made one change to its institutional ratings scale within the last three years. The change occurred July 9, 2002 and the corresponding scales are reproduced below.

**D.A. Davidson & Co. Institutional Research Rating Scale (beginning 7/9/02)**  
Buy, Neutral, Underperform

**D.A. Davidson & Co. Institutional Research Rating Scale (6/18/01 – 7/9/02)**  
Strong Buy, Buy, Neutral, Underperform

PUGET ENERGY INC					
Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	01-Sep-2005	22.90	24.00
14-Feb-2003	19.44	BUY	22-Feb-2005	22.88	23.00
26-Dec-2002	22.10	NEUTRAL	27-Dec-2004	24.52	24.00
			25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00
			26-Dec-2002	22.10	23.00

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

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# Puget Energy

## 3Q05 EPS Reported as Preannounced

- PSD reported 3Q05 EPS of \$0.06, consistent with the company's preannouncement on October 26, 2005, included in PSD's disclosure of its 15 million share equity offering. A year-over-year decline in EPS was driven by higher O&M and D&A, partially offset by better energy margins and lower taxes.
- PSD's utility subsidiary, Puget Sound Energy, is targeting a rate case filing in early 2006 with rates targeted to be effective January 1, 2007. The company intends to address a number of issues in the case including the current lag in recovery of certain costs, a revised/new Power Cost Adjustment (PCA) mechanism, and the addition of new wind projects to rate base.
- On its conference call, management reiterated that it is continuing work to divest InfrastruX as soon as it can. However, it now appears possible that a divestiture could be delayed into 2006 rather than the previously expected timing of year end 2005.
- PSD reiterated 2005 guidance of \$1.30-1.40 as well as 2006 guidance of \$1.40-1.55. The stock is trading at 15.1x 2006E EPS, about inline with the group average of 14.4x. We also do not expect Puget to offer investors material earnings growth in the near-term; however, we expect its dividend yield of 4.8%, well above the group average of 4.0%, to likely support the stock. Accordingly, we believe Puget could be an attractive investment for investors interested in income generation, but we expect the shares to perform inline with their peers.

### Puget Energy (PSD;PSD US)

	2004A	2005E	2006E
EPS (\$)			
Q1 (Mar)	0.67	0.70A	
Q2 (Jun)	0.16	0.15A	
Q3 (Sep)	0.11	0.06A	
Q4 (Dec)	0.61		
FY	1.60	1.40	1.40
P/E FY	13.2	15.1	15.1

Source: Company data, Reuters, JPMorgan estimates.

**Neutral**

**\$21.10**

01 November 2005

### Electric Utilities & IPPs

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### Company Data

Price (\$)	21.10
Date Of Price	01 November 05
52-week Range	20.5 - 24.81
Mkt Cap (\$ mn)	2,426.50
Fiscal Year End	Dec
Shares O/S (mn)	115
Div. Yield	4.8%

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## Valuation and Rating Analysis

We are maintaining our Neutral rating as Puget Energy appears to continue to struggle with regulatory lag and other factors that are preventing its core utility EPS power from emerging. We expected Puget to offer investors potentially modest earnings growth, if any, in 2006 given that its recent sizeable equity offer results in significant EPS dilution in 2006. Longer-term, we believe Puget may still have the potential to offer investors an attractive EPS growth profile; however, it appears that the company's struggle to earn its allowed ROE may prevent the potential EPS growth from investing in its utility from being realized for at least the next several quarters. We expect the company's above average dividend to support the shares, and the shares are trading just above the group average multiple of 14.4x 2006E EPS. Furthermore, if the company is able to address some of the issues masking its core utility earnings power, the shares appear attractively valued. For example, if the company is able to address \$0.11 of regulatory lag it is currently suffering by 2006, we estimate that the company could earn about \$1.50-1.55 in 2006, which would imply that the stock is trading at about 13.5x 2006E EPS, a discount to the group average 2006 multiple, especially given the company's above average yield. We believe this profile could ultimately prove attractive, but we expect the stock to trade inline with the group for the next several quarters because we do not believe visibility on potential EPS improvement will emerge over that time frame.

## Risks to Our Rating

Our Neutral rating on Puget shares is based on what we expect to be EPS dampened by regulatory lag and common share dilution for at least the next several quarters. This results in the company underearning its allowed ROE. If Puget continues to suffer from additional underearning pressure, or inability to add its planned utility investment to rate base, we would expect EPS, and thus the shares, to suffer. On the other hand, as we discussed above, if Puget is able to address its regulatory lag, we believe the shares appear attractive on a relative valuation. As we also discussed above, we expect visibility on this issue to take several quarters to emerge. If Puget is able to address its lag sooner rather than later, investors could get earlier visibility on higher EPS in 2006 and the shares could outperform.



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North America Equity Research  
 02 November 2005

**Companies Recommended in This Report (as of COB 01 November 2005)**

Puget Energy (PSD/\$21.10/Neutral)

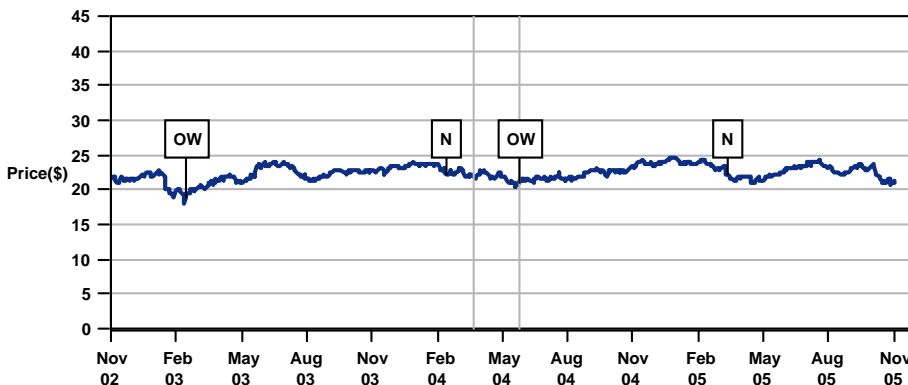
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Puget Energy (PSD) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
13-Feb-03	OW	19.00	-
12-Feb-04	N	22.31	-
25-May-04	OW	21.14	-
14-Mar-05	N	22.15	-

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.  
 Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts' discretion.  
 JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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North America Equity Research  
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IB clients*	46%	45%	39%
JPMSI Equity Research Coverage	34%	49%	17%
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\*Percentage of investment banking clients in each rating category.

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North America Equity Research  
02 November 2005

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02 November 2005

□  
Exhibit No. \_\_\_(BAV-5)  
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11.02.2005

**Puget Energy, Inc. (PSD)**

**No Big Surprises in Q3**

**\$20.83 | BUY**

- **Puget Energy reported Q3 earnings of \$0.06 per share, in line with preliminary results announced last week.**
- **Wind farm projects moving forward smoothly and as expected.**
- **Recent equity offering reduces wind farm-related debt.**
- **EPS guidance for 2005 and 2006 remains unchanged. Our rating remains Buy.**

52 Week High	\$24.81
52 Week Low	\$20.50
P/E	FY04A 12.4x
	FY05E 15.3x
	FY06E 14.1x
12 Mo. Price Target	\$26.00
Shares Out (Mil)	100.29
Market Cap (Bil)	\$2.09
Avg Daily Vol (000s)	291.7
Equity Ratio	43%
Book Value	\$16.29
Dividend	\$1.00
Yield	4.80%
3- 5 yr EPS Growth	3%
Fiscal Year End	Dec

EPS ESTIMATES

FY04A	\$1.55
FY05E	\$1.36
FY06E	\$1.48

▲ Puget Energy reported the details of their Q3 operating earnings per share. The detailed report follows last week’s announcement of a 15 million share secondary stock offering, Q3 EPS of \$0.06, and affirmation of 2005 guidance of \$1.30 to \$1.40 per share.

Q3 operating earnings were \$0.06 per share on continuing operations. This compares to \$0.09 per share in the third quarter a year ago. Earnings for this seasonally weak quarter were impacted by higher O&M costs and plant depreciation expense, partly offset by higher utility energy margins and a decrease in property and income taxes. Electric volumes increased 1.5% year over year, whereas gas volumes increased 1.3%.

InfrastruX remains a discontinued operation, although plans to divest by year end may be slipping into 1Q06. Carrying value of the InfrastruX equity at the end of the third quarter was \$34.3 million.

The 150 MW Hopkins Ridge wind farm is generating test energy and is expected to be on line for the winter peak season. The power cost only rate case for this project was settled uncontested and approved by the WUTC in October.

Construction has started on the 230 MW Wild Horse wind farm project. Costs for this project are expected to be included in the general rate case, which is to be filed in February of 2006. Completion of the project and completion of the general rate case should both occur by year-end 2006. We would note that the power cost tracker will be discussed in the general rate case, and will likely be modified for 2007.

Last week’s 15 million share equity offering brought in \$310 million in proceeds, which the company plans to use to pay down short term debt and fund expenditures associated with the Wild Horse project. Short term debt at the end of the quarter was \$223 million, not including \$46 million in current portion of long term debt. The equity ratio at the end of the year should be 43%, approximately in line with the rate case goal.

Management reiterated earnings guidance for both 2005 and 2006. Guidance for 2005 remains \$1.30 to \$1.40 per share. For 2006 guidance remains at \$1.40 to \$1.55 per share. Note the 2006 guidance includes dilution from the recent equity offering. Our earnings estimates remain unchanged at \$1.36 for 2005 and \$1.48 for 2006.

While rising interest rates have been weighing on the sector, we continue to view PSD as a comparatively low-risk utility, trading at a reasonable value. We are maintaining our Buy rating.

**Additional required disclosures under NASD Rule 2711 are provided on the last page of this document.**

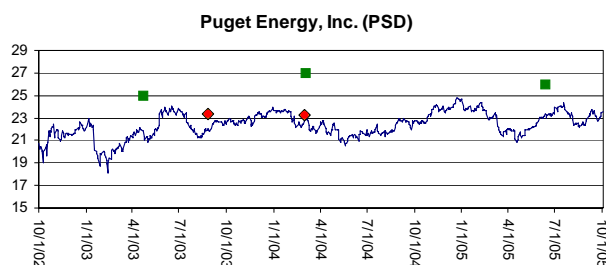
**Required Disclosures:**

Paul C. Latta, CFA, [platta@mwrinc.com](mailto:platta@mwrinc.com), (206) 664-8897

- I, Paul C. Latta, hereby certify (1) that the views in this research note accurately reflect my personal views about any or all of the subject securities or issuers referred to in this note and (2) no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views in this note.

As of September 30, 2005

	From	To	Date	Price
■	Price Target	\$27 to \$26	3/11/2005	\$22.25
■	Price Target	\$25 to \$27	12/1/2003	\$23.48
◆	Added to Focus List		11/26/2003	\$23.21
●	Hold to	Buy	11/26/2003	\$23.21
◆	Removed from Focus List		5/28/2003	\$23.40
●	Buy to	Hold	5/28/2003	\$23.40
■	Price Target	To \$25	1/16/2003	\$20.24



● Ratings Change ◆ Focus List Change ■ Target Price Change

Price targets are subject to change as new information becomes available, and reflect our current judgment regarding this security. Note that there are risks that may impede the achievement of a predicted price target. Price targets are based on fundamental factors such as historical and projected earnings, cash flow, discounted cash flow, relative book value, peer group evaluation, relative sector valuations, and expectations on general market and economic conditions.

McAdams Wright Ragen employs a Ratings System (in effect since 6/12/2002), defined as follows.

Buy/Addition to InStock Recommended List: We expect the Stock to Outperform the Market.

Hold/Addition to InStock Recommended List: We expect the Stock to be a Market Performer.

Sell/Removal from InStock Recommended List: We expect the Stock to Underperform the Market.

Ratings System in effect between 2/7/2002 and 6/12/2002: Strong Buy, Buy, Hold, Underperform, Sell.

Ratings System in effect prior to 2/7/2002: Buy, Moderate Buy, Hold, Underperform, Sell.

	Percentage of Rated Stocks Currently Assigned this Rating	Percentage of Rated Stocks with this Rating with which MWR has had an Investment Banking Relationship in the last 12 months
Buy	54%	6%
Hold	42%	7%
Sell	4%	0%

For Price Chart and Ratings History disclosures, please go to <http://www.mwrinc.com/ClientAccess/quotesresearch.html>, or to request information, please contact Jason T. Kunkel, Research Assistant, (206) 664-8854, [mwr@mwrinc.com](mailto:mwr@mwrinc.com)

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**Additional required disclosures under NASD Rule 2711 are provided on the last page of this document.**

# Puget Energy, Inc.

## PSD: Higher Operating Expenses Result in Lower Q3, Maintain Market Perform

**Summary:** PSD reported Q3 results of \$0.06 compared to \$0.11 the prior year. The shortfall was primarily due to higher operating expenses. The Utility division reported EPS of \$0.06 compared to \$0.10 the prior year. The InfrastruX division, which was classified as discontinued business, had no impact this quarter compared to \$0.01 the prior year. We are maintaining our FY'05 and FY'06 EPS estimates of \$1.36 and \$1.50, respectively, and our Market Perform rating.

- **Total revenues increased 8.7% to \$490.4 million mainly due to rate increases.** Electric margins were essentially flat at \$149.7 million. Gas margins increased \$4.4 million primarily as a result of rate increases and higher usage. Weather was 11% warmer than normal and flat with last year. Customer growth for the LTM ending September 2005 was approximately 2% for electric and approximately 3% for natural gas.
- **Operation and maintenance expenses increased 21.7% to \$81.6 million due to planned maintenance.** D&A increased approximately 5.1% to \$60.6 million due to infrastructure additions. Interest expense increased 4.8% to \$43.0 million due to higher debt.
- **InfrastruX broke even this quarter compared to \$0.01 the prior year.** The Company intends to sell this division and has approximately \$34 million equity in this division at the end of the third quarter.
- **PSD was granted the power cost only rate case request of \$55.6 million,** which also included the Hopkins Ridge investment of \$190 million. As part of the settlement, the Company is expected to file a general rate case in February 2006 and request the inclusion of the Wild Horse investment and increased power costs in rates.
- **The Company maintained its \$1.30-\$1.40 and \$1.40-\$1.55 guidance for 2005 and 2006, respectively. In October 2005, PSD issue 15 million shares generating \$310 in net proceeds which should be used to repay debt and finance the wind project.**

### Valuation

PSD stock is currently trading at 15.4x our FY'05 estimate of \$1.36 and 14.0x our FY'06 estimate of \$1.50, which is in line with the peer group average. On EV/EBITDA basis, the stock is trading at 7.4x or at a discount to the peer group average of 8.4x. On price-to-book basis, the stock is trading at 1.3x discount to the peer group average of 1.8x. Its dividend yield is 4.7% compared to 4.01% peer group average. We are maintaining our Market Perform rating and would be more bullish on any pull back.

### Regional Growth November 3, 2005

**Puget Energy Inc  
 PSD/NYSE  
 Intraday Price on 11/3/05: \$21.00  
 Market Perform**

**Selman Akyol  
 314-342-2158  
 akyols@stifel.com**

**Vishal Sharma  
 314-342-2164  
 sharmav@stifel.com**

52-Week Range	\$20.73 – \$24.81
Average Daily Volume	333,758
Shares Outstanding	115 million
Market Capitalization	\$2.1 billion
Market Cap./2005E Revenue	0.8x
Long Term Debt (Mil)	\$2,306
Total Debt / Total Capitalization	58%
Institutional Ownership	49%
Trailing 12 mo. Revenue	\$2,434 million
Book Value per Share (09/05)	\$16.60
Long-Term Projected EPS Growth	5%
Dividend	\$1.00
Dividend Yield	4.7%

### Annual Estimates

FY (Dec)	2003A	2004A	2005E	2006E
Revs (Mil)	\$2,041	\$2,199	\$2,532	\$2,728
% chg y/y	2%	8%	15%	8%
<b>EPS</b>	<b>\$1.22</b>	<b>\$0.55*+</b>	<b>\$1.36</b>	<b>\$1.50</b>
Street	-	-	\$1.38	\$1.60
Price/EPS	17.2x	NMF	15.4x	14.0x

### Quarterly EPS Estimates

FY (Dec)	Mar	Jun	Sep	Dec
2005E	\$0.71A	\$0.14A	\$0.06A	\$0.45
Street	-	-	-	\$0.51
2004A	\$0.67	(\$0.07)*	\$0.11	(\$0.16) <sup>+</sup>
2003A	\$0.45	\$0.22	\$0.10	\$0.45

\*Includes a \$0.28 charge related to Tenaska Order

<sup>+</sup>Includes a \$0.77 charge related to goodwill impairment

**Required Disclosures: C-2  
 See Page 5 for Required Disclosures**

### Equity Research

1125 17th Street  
 Suite 1600  
 Denver, CO 80202  
 800-525-9899

**Third Quarter Highlights**

PSD reported third quarter results of \$0.06 compared to \$0.11 the prior year. Typically Q3 is the lowest of quarters in terms of earnings due to seasonality. Total revenues increased 8.7% to \$490.4 million. Electric revenues increased 8.6% to \$375.0 million mainly as a result of a \$12.8 million increase due to the rate case and a \$4.5 million increase due to higher usage. The number of electric customers increased approximately 2% in the last twelve months. Electric revenues increased \$7.7 million due to sales of non-core gas purchased for generation. Electric margins were essentially flat at \$149.7 million. Gas revenues increased 8.0% to \$111.0 million as a result of a \$13.8 million PGA in 2005, a \$2.4 million increase due to the rate case, and a \$2.5 million increase due to increased usage. Gas customers increased approximately 3% since the third quarter last year. Gas margins increased to \$38.7 million from \$34.3 million as a result of the rate increases and increased usage. Weather, as measured by heating degree days, was 11% warmer than normal and essentially flat with the prior year. Operations and maintenance expenses increased 21.7% to \$81.6 million due to planned maintenance. D&A increased approximately 5.1% to \$60.6 million due to infrastructure additions. Taxes other than income taxes increased 4.9% to \$44.8 million due to higher revenues and property taxes. Operating income decreased 5.6% to \$47.5 million. Interest expense increased 4.8% to \$43.0 million due to higher debt. InfrastruX broke even this quarter. Net income was \$5.9 million compared to \$11.1 million last year, and the diluted shares outstanding were approximately 1% higher compared to last year.

**InfrastruX**

As of the quarter end, PSD had approximately \$34 million in net equity and approximately \$165 million in net debt in its non-regulated business, InfrastruX. During the quarter, InfrastruX broke even compared to \$0.01 last year. The Company reiterated its intention to monetize this business by the end of this year. For the quarter, the division generated \$7.5 million in EBITDA compared to \$13.7 million last year. For the full year, the \$40-\$45 million EBITDA guidance remains unchanged. Assuming a 6-8 multiple would imply an equity value of \$75 to \$195 million. We would anticipate the Company reducing debt with the net proceeds pending any other uses.

**Balance Sheet**

Total Long-Term Debt at the end of September was \$2.3 billion or 58% of the total capital. The Company incurred approximately \$179 million in cap ex in Q3'05 and \$416 million for the first nine months this year. PSD guided that its cap ex on the two wind projects approximately \$570 million, \$190 million of which will be used on Hopkins Ridge and \$380 on the Wild Horse wind power project. The energy delivery (transmission and distribution) cap ex is estimated to be \$400 million in 2005, \$445 million in 2006, and \$475 million in 2007. In October 2005, PSD sold 15 million shares generating \$310 million in net proceeds which should be used to pay down debt and the wind project. The Company expects the equity ratio to reach 43% by the year end.

**Outlook**

The Company's power cost only rate case (PCORC) request was granted resulting in an annual revenue increase of approximately \$56 million. As part of the settlement, PSD is required to file a general rate case in February 2006. Management noted that it would request recovery of the Wild Horse investment along with the increased power costs in its rates. We expect a decision on that case by the end of next year. We remind that the Hopkins Ridge investment was already included in the PCROC request. This project is expected to go online in 2006. The Company expects to generate sufficient cash from its operations to finance its energy delivery (transmission and distribution) cap ex. With the issue of 15 million shares, PSD does not expect to issue anymore equity in the near term. The sale of InfrastruX should also provide the Company with additional cash.

Despite the additional shares, the Company maintained its earlier guidance of \$1.30-\$1.40 for 2005 and \$1.40-\$1.55 for 2006. These estimates are based on normal weather assumptions and do not include stock option expenses. As a result, we are maintaining our \$1.36 for 2005 and \$1.50 for 2006.



**Valuation**

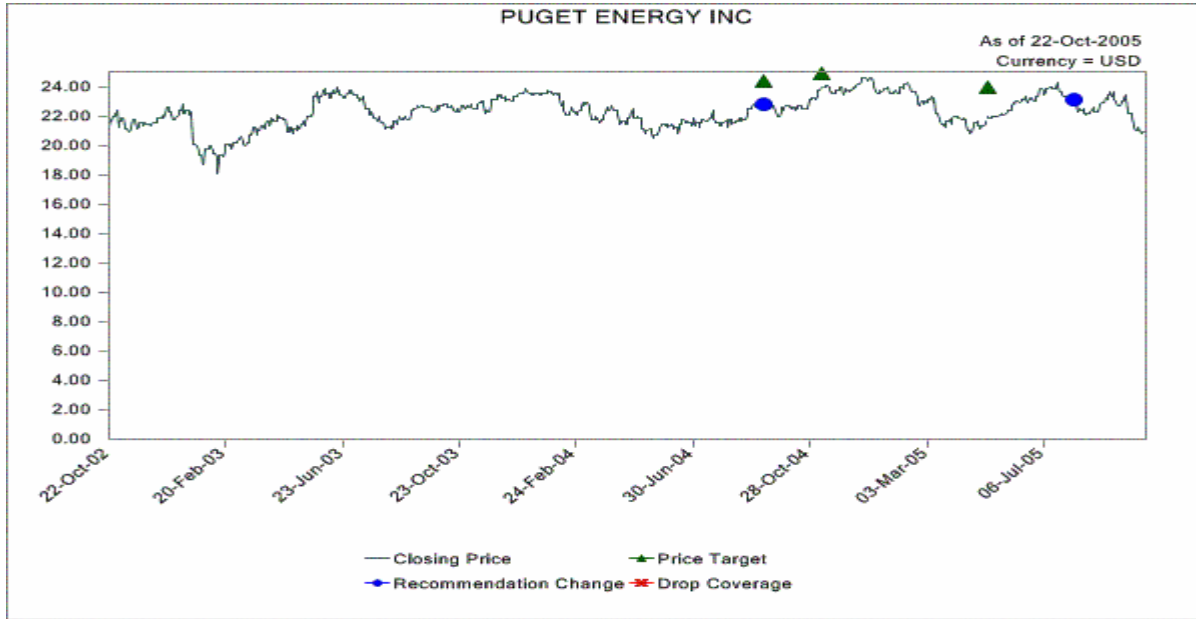
PSD stock is currently trading at 15.4x our FY'05 estimate of \$1.36 and 14.0x our FY'06 estimate of \$1.50, which is in line with the peer group average. On EV/EBITDA basis, the stock is trading at 7.4x or at a discount to the peer group average of 8.4x. On price-to-book basis, the stock is trading at 1.3x discount to the peer group average of 1.8x. Its dividend yield is 4.7% compared to 4.01% peer group average. At current price levels, we believe the price essentially reflects the growth opportunities. The general rate case to be filed in 2006, would essentially impact 2007. Next year the Hopkins wind project would come online. In the long run, the addition of low cost wind power in its portfolio could provide cost advantage to the Company. For now, we are maintaining our Market Perform rating and would be more bullish on any pull back.



# Required Disclosures

Exhibit No. \_\_\_(BAV-5)

**EFFECTIVE NOVEMBER 13, 2002, STIFEL NICOLAUS ELIMINATED PRICE TARGETS ON PERFORM-RATED STOCKS. ALL MARKET OUTPERFORM AND MARKET UNDERPERFORM-RATED STOCKS CONTINUE TO HAVE PRICE TARGETS.**



**PUGET ENERGY INC**

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
04-Aug-2005	23.17	MARKET PERFORM	04-May-2005	21.77	24.00
09-Sep-2004	22.88	MARKET OUTPERFORM	08-Nov-2004	24.05	25.00
			09-Sep-2004	22.88	24.50

*We, the research analysts responsible for this report, attest that the views expressed in this research report accurately reflect our personal views about any and all of the subject securities or issuers. We have not received, and will not receive, compensation in return for the specific recommendations or views expressed by us in this report.*

**KEY FOR DISCLOSURES:** A – Stifel, Nicolaus makes a market in the common stock of this company. B – The analyst owns the common stock of this company. B-1 – A member of the analyst’s household owns the common stock of this company. C – Stifel, Nicolaus has managed or co-managed a public offering of securities for this company within the past 12 months. C-1 – Stifel, Nicolaus has been compensated for investment banking services by this company within the past 12 months. C-2 – Stifel, Nicolaus intends to seek compensation for investment banking services from this company in the next 3 months. D – The analyst serves on the Board of Directors of this company. D-1 – A member of the analyst’s household serves on the Board of Directors of this company. E – Stifel, Nicolaus beneficially owns in excess of 1% of a class of common equity securities of this company.

**RATING SYSTEM:** Market Outperform – The total return of the stock, adjusted for risk, is expected to outperform the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Perform – The total return of the stock is expected to perform in line with the broad U.S. equity market, defined by the Russell 2000, over the next 12 months. Market Underperform – The total return of the stock is expected to Underperform the broad U.S. equity market, defined as the Russell 2000, over the next 12 months. The security should be sold if such sale is consistent with clients' needs and objectives. Our 12-month price targets may temporarily vary from these expectations due to market volatility.

**RESEARCH COVERAGE:** As of September 30, 2005, Stifel Nicolaus had 221 companies under coverage. Stifel Nicolaus rated 93 companies, or 42%, as Market Outperform/“Buy,” 125 companies, or 57%, as Market Perform/“Hold,” and 3 companies, or 1%, as Market Underperform/“Sell.” During the previous 12 months, Stifel Nicolaus provided investment banking services for 16 of the companies rated Market Outperform/“Buy” (17%), 16 of the companies rated Market Perform/“Hold” (13%), and 1 of the companies rated Market Underperform/“Sell” (33%).

The information and statistical data contained herein have been obtained from sources we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to any changes in figures or our views.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST. Please contact the analyst for further information. Stifel, Nicolaus & Company, Inc. research is also available online at [www.multex.com](http://www.multex.com) and [www.firstcall.com](http://www.firstcall.com).

This is not a solicitation of any order to buy or sell.

## UBS Investment Research

# Puget Energy Inc.

## Regulatory Issues Continue to Depress Despite Decent Quarter

### ■ Beat Expectations Despite Year-over-Year Decline

Puget realized a 33% decrease in recurring 3Q EPS, to \$0.06 from \$0.09 in 3Q04. The results were \$0.03 above our est. of \$0.03 and \$0.02 above the Street consensus est. of \$0.04. The variance from our est. was driven by stronger than expected usage at the utility. Year-over-year results were mainly driven down by higher O&M and reliability costs at the utility.

### ■ Maintaining 2005 and Reducing 2006 Estimates

On October 26th, Puget announced the sale of 15 million shares of common stock. We anticipated dilution but the magnitude was a bit higher than expected. While maintaining our '05 EPS est. at \$1.40, we are lowering our '06 est. to \$1.45 from \$1.50.

### ■ Outstanding Issues

Puget has several outstanding regulatory issues that we believe will serve as a stock overhang. These include rate recovery on delivery capex, rate recovery of the Wild Horse Wind Farm investment, and the future of the PCA mechanism after July 2006.

### ■ Valuation: Maintaining Price Target at \$23

Our PT is derived using DCF analysis and implies a 15.9x PE on our recurring 2006 EPS. Price appreciation to \$23, combined with its 4.8% yield, represents a potential total return of 14.5%.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	2,383	2,569	2,186	2,383	-
EBIT	377	418	395	447	-
Net income (UBS)	110	155	142	171	-
EPS (UBS, US\$)	1.16	1.55	1.40	1.45	-
Net DPS (UBS, US\$)	1.00	1.00	1.00	1.00	-
Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	16.3	18.1	18.8	-
ROIC (EBIT) %	-	13.0	12.3	12.6	-
EV/EBITDA x	-	6.9	7.0	6.6	-
PE (UBS) x	-	14.6	15.0	13.5	-
Net dividend yield %	-	4.4	4.8	4.8	-

Source: Company accounts, Thomson Financial, UBS estimates. UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$20.97 on 03 Nov 2005 19:41 EST

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Americas	
Electric Utilities	
<b>Rating</b>	<b>Neutral 2</b> <i>Unchanged</i>
<b>Price target</b>	US\$23.00 <i>Unchanged</i>
<b>Price</b>	US\$20.97

RIC: PSD.N BBG: PSD US

**4 November 2005**

#### Trading data

52-wk. range	US\$24.73-20.70
Market cap.	US\$2.09bn
Shares o/s	99.9m
Free float	80%
Avg. daily volume ('000)	278
Avg. daily value (US\$m)	6.2

#### Balance sheet data 12/05E

Shareholders' equity	US\$1.72bn
P/BV (UBS)	1.2x
Net cash (debt)	(US\$2.60bn)

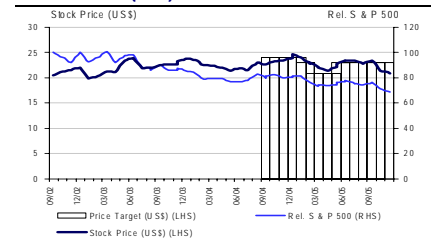
#### Forecast returns

Forecast price appreciation	+9.7%
Forecast dividend yield	4.8%
Forecast stock return	+14.5%
Market return assumption	9.5%
Forecast excess return	+5.0%

#### EPS (UBS, US\$)

	12/05E		12/04	
	From	To	Cons.	Actual
Q1	0.68	0.68	<i>0.72</i>	0.67
Q2	0.12	0.14	<i>0.14</i>	0.16
Q3	0.03	0.06	<i>0.04</i>	0.11
Q4E	0.54	0.52	<i>0.52</i>	0.52
12/05E	1.40	1.40	<i>1.38</i>	
12/06E	1.50	1.45	<i>1.48</i>	

#### Performance (US\$)



Source: UBS  
[www.ubs.com/investmentresearch](http://www.ubs.com/investmentresearch)

**This report has been prepared by UBS Securities LLC**

### ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 4

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## Earnings Summary

Puget realized a 33% decrease in recurring third quarter EPS, to \$0.06 from \$0.09 in 3Q04. The results were \$0.03 above our estimate of \$0.03 and \$0.02 above the Street consensus estimate of \$0.04. The variance to our estimate was driven by stronger than expected usage at the utility. Year-over-year results were mainly driven down by higher O&M and reliability costs at the utility.

Management maintained its recurring 2005 EPS guidance of \$1.30 – 1.40 as well as its recurring 2006 guidance of \$1.40 – 1.55.

## Our View

While third quarter results beat our estimates, we remain cautious given the regulatory overhang for the company. Major issues continue to be the recovery of current delivery capex, recovery of the Wild Horse Wind Farm investment and treatment of the Power Cost Adjustment (PCA) Mechanism post July 2006. The company expects to file for a general rate case in February of 2006, to address its delivery capex under-recovery and PCA Mechanism. The recent approval for recovery of \$55.6 million of higher power costs also included recovery for the company's first wind farm at Hopkins Ridge. We expect this case to be completed by year-end 2006.

## Key 3Q05 Drivers

**Puget Sound Energy (PSE)**, the utility, realized a 33% decrease in third quarter recurring EPS, to \$0.06 from \$0.09 in 3Q04. The decrease was led by higher O&M expense (\$0.08) due to expenses associated with the generation fleet and ongoing transmission reliability initiatives, and higher utility depreciation expense (\$0.02) due to the completion of a gas plant. Partial offsets were from higher gas margins (\$0.03) due to a more favorable customer mix, decreased property and income taxes (\$0.02) and other (\$0.02).

Electric retail sales increased 1.5% due to customer growth. Residential, commercial and industrial sales increased 1.4%, 1.0% and 0.2%, respectively. Gas volumes increased 1.3% led by higher industrial and commercial volumes of 9.1% and 4.2%, respectively. Residential gas sales rose 0.8% for the quarter, while the transportation segment fell 2%.

## Maintaining 2005 and Reducing 2006 Estimates

On October 26th, Puget announced the sale of 15 million shares of common stock. We anticipated the dilution though the magnitude was a bit higher than expected. While maintaining our '05 EPS estimate at \$1.40, we are lowering our '06 estimate to \$1.45 from \$1.50.

## Maintaining Price Target at \$23

Our 12-month price target of \$23 is derived using a DCF analysis. This implies a 15.9x PE on our recurring 2006 EPS.

Price movement to \$23 per share, combined with the current \$1.00/share annual dividend (or 4.8% yield), suggests a 14.5% total return potential.

---

### ■ Puget Energy Inc.

Puget Energy, Inc. is an energy services holding company incorporated in the state of Washington. All of its operations are conducted through its subsidiaries, Puget Sound Energy, Inc. (PSE), a utility company, and InfrastruX Group, Inc. (InfrastruX), a construction services company. PSE furnishes electric and gas service in a territory covering 6,000 square miles, principally in the Puget Sound region of Washington State. Puget has decided to exit the InfrastruX business and classifies it as discontinued operations.

### ■ Statement of Risk

Investors should be aware that PSE is short power and purchases a proportion of its power requirement in the spot market. This exposes the utility to volatile power costs - a grave concern given that PSE does not have a complete fuel pass-through. PSE has a power tracker mechanism in place that shares power costs / savings with customers in a specified manner. The utility absorbs the first \$40 million of the excess power costs, beyond which the customers bear 99% of the excess. However, this mechanism expires in July 2006 and it is uncertain in what form it would get renewed.

It is also important to note that PSE relies on hydro for roughly 27% of its total power requirement. While hydro is a cheap fuel source, it comes with a high degree of volatility since it is highly dependent on the weather and, more specifically, on the stream flow. This introduces fuel cost volatility that forces PSE to purchase electricity in the spot market in the event the company faces a low hydro year.

To address the short power situation, PSE is embarking on a \$1.3 billion generation acquisition program that will add 1,500 MW over the next 8 years. While this plan is integral to Puget's growth strategy, it introduces significant execution risks. These include the availability of generation assets, pricing, integration of the new acquisitions, and negotiating a working relationship with co-owners on partial ownership acquisitions.

Investors should also be aware of the potential impact of weather on Puget's regulated utility sales and the impact of soft patches in the economy. As a regulated entity, PSE faces regulatory risks. Finally, Puget's senior debt is currently rated BBB- and Ba1 by S&P and Moody's, respectively. While Puget does not have any rating downgrade triggers that would accelerate the maturity dates of its outstanding debt, a rating downgrade could adversely impact its ability access the capital markets.

#### ■ Analyst Certification

Each research analyst primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.

## Required Disclosures

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### UBS Investment Research: Global Equity Ratings Definitions and Allocations

UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	37%	35%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	50%	32%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	13%	28%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 30 September 2005.

#### KEY DEFINITIONS

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

**Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

**Rating/Return Divergence (RRD)** This qualifier is automatically appended to the rating when stock price movement has caused the prevailing rating to differ from that which would be assigned according to the rating system and will be removed when there is no longer a divergence, either through market movement or analyst intervention.

#### EXCEPTIONS AND SPECIAL CASES

**US Closed-End Fund ratings and definitions are:** Buy: Higher stability of principal and higher stability of dividends; Neutral: Potential loss of principal, stability of dividend; Reduce: High potential for loss of principal and dividend risk.

**UK and European Investment Fund ratings and definitions are:** Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Reduce: Negative on factors such as structure, management, performance record, discount.

**Core Banding Exceptions (CBE):** Exceptions to the standard +/-10% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Companies Mentioned table in the relevant research piece.



Companies mentioned

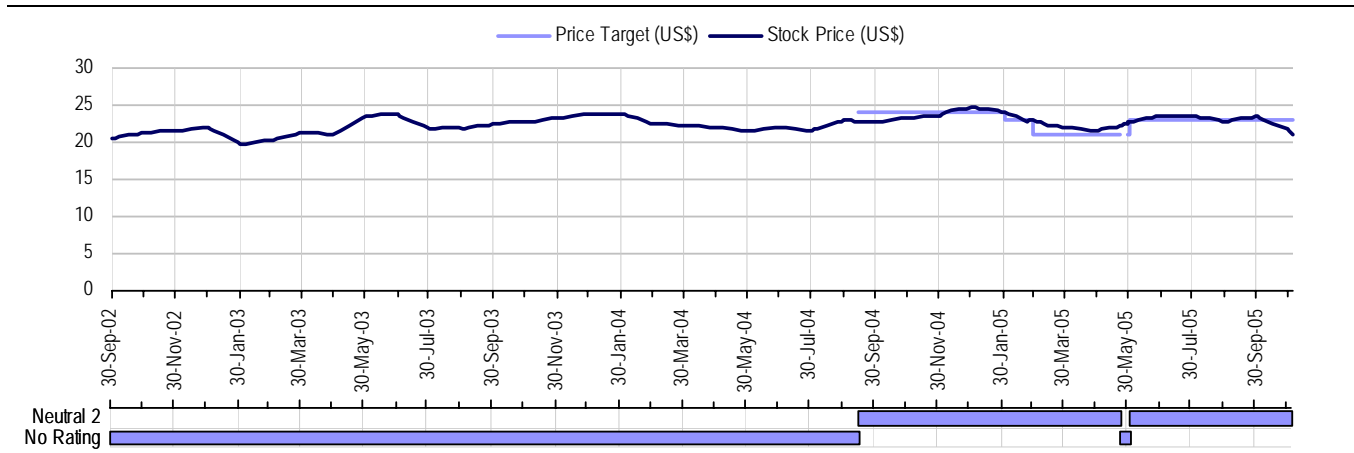
Company Name	Reuters	Rating	Price	Price date/time
Puget Energy Inc. <sup>2,4,5,6a,6b,6c,7,16</sup>	PSD.N	Neutral 2	US\$20.97	03 Nov 2005 19:41 EST

Source: UBS. EST: Eastern standard time.

2. UBS AG, its affiliates or subsidiaries has acted as manager/co-manager in the underwriting or placement of securities of this company or one of its affiliates within the past 12 months.
4. Within the past 12 months, UBS AG, its affiliates or subsidiaries has received compensation for investment banking services from this company/entity.
5. UBS AG, its affiliates or subsidiaries expect to receive or intend to seek compensation for investment banking services from this company within the next three months.
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7. Within the past 12 months, UBS Securities LLC has received compensation for products and services other than investment banking services from this company.
16. UBS Securities LLC and/or UBS Capital Markets LP makes a market in the securities and/or ADRs of this company.

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

Puget Energy Inc. (US\$)



Source: UBS; as of 3 November 2005.

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NOVEMBER 16, 2005

UTILITIES

# Puget Energy, Inc.

NYSE-PSD

## 3Q05 Results In Line

 ANALYST OPINION: **SELL**

### PRIMARY STOCK STATISTICS

FY End	Dec
52-Week Range	\$25-\$21
Market Cap (billion)	\$2.34
TTM Revenue (billion)	\$2.64
Shares Outstanding (million)	115.5
Book Value	\$15.96
Dividend/Yield	\$1.00/4.3%
Est. Sec. EPS Grth Rate	5%

 PRICE: **\$20.50**

 PRICE TARGET: **NA**

### EARNINGS ESTIMATES

Current Quarter

PRIOR	CURRENT	P/E
-	-	-
-	\$1.22	16.8x
-	\$1.26	16.3x
\$1.35	\$1.35	15.2x
-	\$1.40	14.6x

### KEY POINTS

- Puget Energy reported 3Q05 normalized EPS of \$0.06 compared to \$0.09 last year. While revenues increased 18%, mostly from rate increases, operating and maintenance expenses increased 22% due primarily to higher maintenance costs.
- InfrastruX earned \$0.00 per share but shows up in discontinued operations as the Company still expects the property to be monetized in 2005. This sale could generate \$50 million plus against \$2.3 billion of debt, in our estimation.
- Management reiterated FY05 guidance at between \$1.30-\$1.40 and 2006 guidance of \$1.40-\$1.55. We have initiated a new FY06 EPS estimate of \$1.40, the low of management's range.
- We are maintaining our Sell rating as we believe there is little earnings leverage here although the dividend is attractive. The forward P/E of 14x is above our peer group average of 12.9x and with equity dilution seen likely over the next few years, a high estimated dividend payout of almost 70%, and a fairly leveraged balance sheet at 58% debt to capital, we continue to feel better yield/growth opportunities lie in names like Exelon.

### SUMMARY AND STOCK OPINION

Puget Energy reported 3Q05 EPS of \$0.06 compared with \$0.09 last year. Revenues increased by 18% due to rate increases and a 1.5% increase in electric sales volume and a 1.3% increase in natural gas volumes. Operating expenses increased by 22% due primarily to higher maintenance costs and higher pension and benefit expense. We expect the trend towards higher O&M and depreciation expenses to continue for the foreseeable future. InfrastruX broke even this quarter and it is still expected that this division will be sold by year-end with proceeds to pay down debt.

After the quarter, Puget sold 15 million shares which generated about \$300 million in net proceeds. Proceeds are to be used to pay down debt which totaled \$2.3 billion at quarter end. Given projected large capital expenditures for the next few years to add generation capacity, we don't expect much de-leveraging of the balance sheet with potential continued dilution for additional equity requirements. While the dividend level is attractive at 4.8% the payout ratio on our FY06 estimate is a relatively high 72%.

(Continued)

Management provided FY06 guidance of between \$1.40 and \$1.50 and as such we are initiating a FY06 EPS estimate of \$1.40.

Trading at 14.6x our FY06 estimate of \$1.40 (and 14x consensus FY06 estimates of \$1.47), a premium to the group probably due to the attractive yield, we feel the stock is somewhat overvalued here given continued large capex requirements, tight cash flows and lack of clarity on the longer-term earnings power with the changing mix of internally generated power.

Peer Comparison

	Ticker	Price	Div. Yield (%)	P/Book	P/Sales	P/EBITDA	P/E (2005)	P/E (2006)
Pinnacle West Capital Corp.	PNW	\$41.02	4.9	1.1	1.3	4.3	13.0	13.3
Xcel Energy Inc.	XEL	\$17.98	4.8	1.3	0.8	3.8	14.7	13.6
Sempra Energy	SRE	\$42.45	2.7	1.8	1.0	6.0	12.4	12.2
Avista Corp.	AVA	\$17.16	3.3	1.1	0.7	3.5	19.3	11.5
PNM Resources Inc.	PNM	\$24.47	3.3	1.3	0.9	5.0	15.6	13.0
MDU Resources Group Inc.	MDU	\$32.92	2.3	2.2	1.2	6.0	15.6	13.7
<b>AVERAGE</b>			<b>3.5</b>	<b>1.5</b>	<b>1.0</b>	<b>4.7</b>	<b>15.1</b>	<b>12.9</b>
Dow Jones Utilities Average	^UTIL	\$391.30	3.3	2.4	1.4	NA	16.2	NA
<b>Puget Energy Inc.</b>	<b>PSD</b>	<b>\$20.54</b>	<b>4.9</b>	<b>1.2</b>	<b>0.8</b>	<b>3.1</b>	<b>15.0</b>	<b>14.0</b>

Source: Factset (11/15/05)

Puget Energy, Inc. is one of Washington state's largest utility companies. Through its subsidiary, Puget Sound Energy, it provides electricity to more than 940,000 customers and provides natural gas to more than 600,000 in western Washington. The company owns some fossil-fueled and hydroelectric plants and its InfrastruX Group specializes in energy management and infrastructure construction services. Headquarters: Bellevue, WA

Other public companies mentioned:

Exelon Corporation (NYSE-EXC-\$50.87, VLI-Buy)

S&P 500: 1231.21

**REQUIRED DISCLOSURES**

Wells Fargo Securities, an affiliate of Wells Fargo Investments, has managed or co-managed a public offering of Puget Energy, Inc. within the last 12 months. The analyst or a member of the analyst’s household has beneficial ownership in the securities of Puget Energy, Inc. in the form of a long position in such securities. Wells Fargo Securities, an affiliate of Wells Fargo Investments, has received compensation for investment banking services from Puget Energy, Inc. in the last 12 months.

**ANALYST CERTIFICATION**

By issuing this research report, each Ragen MacKenzie analyst whose name appears on the front page of this research report hereby certifies that: (i) the recommendations and opinions expressed in the research report accurately reflect the research analyst’s personal views about any and all of the subject securities or issuers discussed herein and (ii) no part of the research analyst’s compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in the research report.

**PRICE TARGET VALUATION METHODOLOGY AND RISKS**

The methods used to determine the price target are generally based on a multiple of earnings, cash flow, revenue and/or historical and relative valuation multiples. Risks that could impede achievement of our price target include, but are not limited to, changes in economic and industry conditions, consumer and business spending patterns, as well as geo-political risks. When a price target is used, please refer to the Valuation and Risks section in the body of the report for additional discussion on the specific valuation methodology and related risk factors as they pertain to this analyst’s investment thesis.

**RATING SYSTEM**

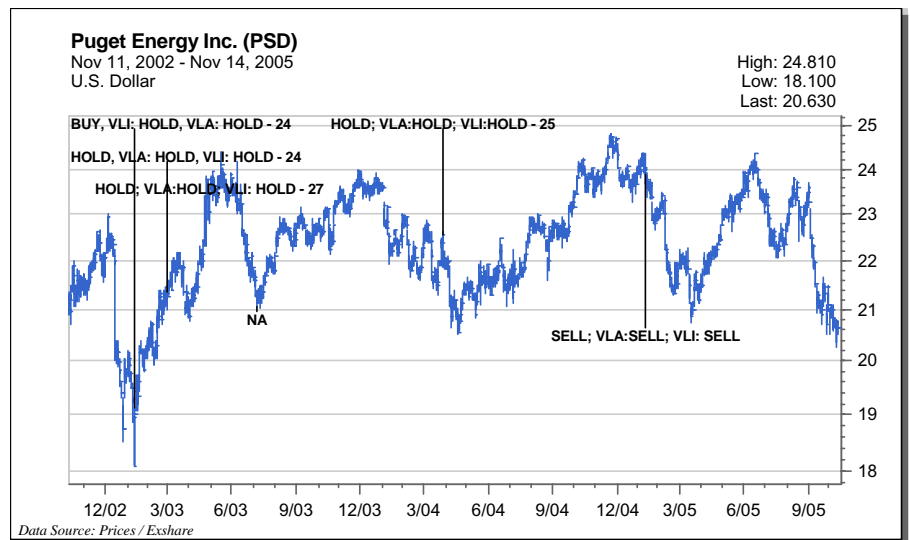
**BUY** – Immediate purchase is recommended; the stock is expected to outperform the general market over the next 12-18 months.  
**HOLD** – Holding the stock is recommended. The stock has moved out of our preferred buying range, but there is further upside to the share price; or stated objectives at the time of purchase have changed and share appreciation may take another 6-12 months.  
**SELL** – The stock has reached the stated price objective and appreciation has been achieved; or certain company fundamentals have changed which warrant investors selling the stock to avoid price decline.

**RATINGS ALLOCATIONS**

Rating	% of covered companies with this rating	% for which IB Services have been provided
<i>Analyst Coverage</i>		
BUY	26%	0%
HOLD	66%	9%
SELL	8%	25%
<i>Value Recommended List—Appreciation</i>		
BUY	36%	0%
HOLD	43%	0%
SELL	21%	0%
<i>Value Recommended List—Income</i>		
BUY	20%	100%
HOLD	80%	25%
SELL	0%	0%
<i>Growth Recommended List</i>		
BUY	57%	0%
HOLD	43%	0%
SELL	0%	0%

Updated on 10/07/2005

**PRICE HISTORY**



The price targets indicated in the chart above may be adjusted for stock splits. Where the price target was originally given as a range, the midpoint of the range has been used.

**OTHER DISCLOSURES**

**INVESTMENT PRODUCTS:**    ▶ **NOT FDIC INSURED**    ▶ **NO BANK GUARANTEE**    ▶ **MAY LOSE VALUE**

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## Utilities

December 1, 2005

### Continuing Coverage with Hold Rating

**Selman Akyol** (314)342-2158 akyols@stifel.com  
**Vishal Sharma** (314)342-2164 sharmav@stifel.com

- In connection with the acquisition of substantially all of the Capital Markets business of Legg Mason Wood Walker, Incorporated by Stifel Financial Corp. (SF - NYSE), we are implementing a three-tiered stock rating system (Buy, Hold, Sell). The rating system is based upon performance relative to the S&P 500.

- We are continuing coverage of Puget Energy, Inc. with a Hold rating.

- Puget Energy, Inc. is an energy services holding company incorporated in Washington in 1999. It serves as the parent company to Puget Sound Energy, Inc. (PSE). PSE, incorporated in Washington, furnishes electric and gas service in a territory spread over 6,000 square miles. As of September 2005, PSE served approximately 1 million electric customers and 683,000 natural gas customers. PSE also generates electricity using hydro-powered, natural gas fired plants and coal plants. This year PSD discontinued its non-regulated business, InfrastruX Group, a utility construction services company, making it a 100% regulated utility.

- PSD has a customer growth of approximately 2% on the electric side and 3% on the natural gas side, both above the national averages. The Company has access to cheap hydro-electric power and has its own generation resources as well. Though PSD enjoys the privilege of passing gas costs and adjusting electric rates for excess power costs, margins were negatively impacted by the higher power costs of acquiring/generating power. The Company has begun venturing into low cost wind energy and expects to recover investments through rate cases.

- PSD is currently trading at 13.9x our FY'06 EPS of \$1.50, essentially in line with the peer group average of 14.3x. On a price-to-book basis, 1.3x compared to 1.7x peer group average, and on EV/EBITDA basis, 7.6x compared to 8.1x peer group average. The stock is currently yielding 4.8% compared to 4.1% peer group average.

### Company Description

Puget Energy, Inc. is an energy services holding company incorporated in Washington in 1999. It serves as the parent company to Puget Sound Energy, Inc. (PSE). PSE, incorporated in Washington, furnishes electric and gas service in a territory spread over 6,000 square miles. As of September 2005, PSE served approximately 1 million electric customers and 683,000 natural gas customers. PSE also generates electricity using hydro-powered, natural gas fired plants and coal plants. In 2005, PSD discontinued its non-regulated business, InfrastruX Group, a utility construction services company, making it a 100% regulated utility.

Changes	From (Previous)	To (Current)
Rating	--	Hold
Target Price	NA	--
FY05E EPS	--	\$1.36
FY06E EPS	--	\$1.50

Stock Data			
Price (11/30/05):			\$20.78
52-Week Range:			\$25 – \$20
Market Cap.(\$mm):			\$2,088.0
Shr.O/S-Diluted (mm):			115.0
Avg Daily Vol (3 Mo):			354,689
Dividend (\$):			\$1.00
Yield (%):			4.8%
Book Value/Share:			\$16.60
S&P Index:			1,249.48

Note: Correction; Wire originally issued on 12/1/05.

EPS (Net)	2004A	2005E	2006E
Q1	\$0.67A	\$0.71A	\$0.75
Q2	(0.07)A	0.14A	0.17
Q3	0.11A	0.06A	0.09
Q4	(0.16)A	0.45	0.49
FY Dec	\$0.55A	\$1.36	\$1.50
P/E	37.8x	15.3x	13.9x

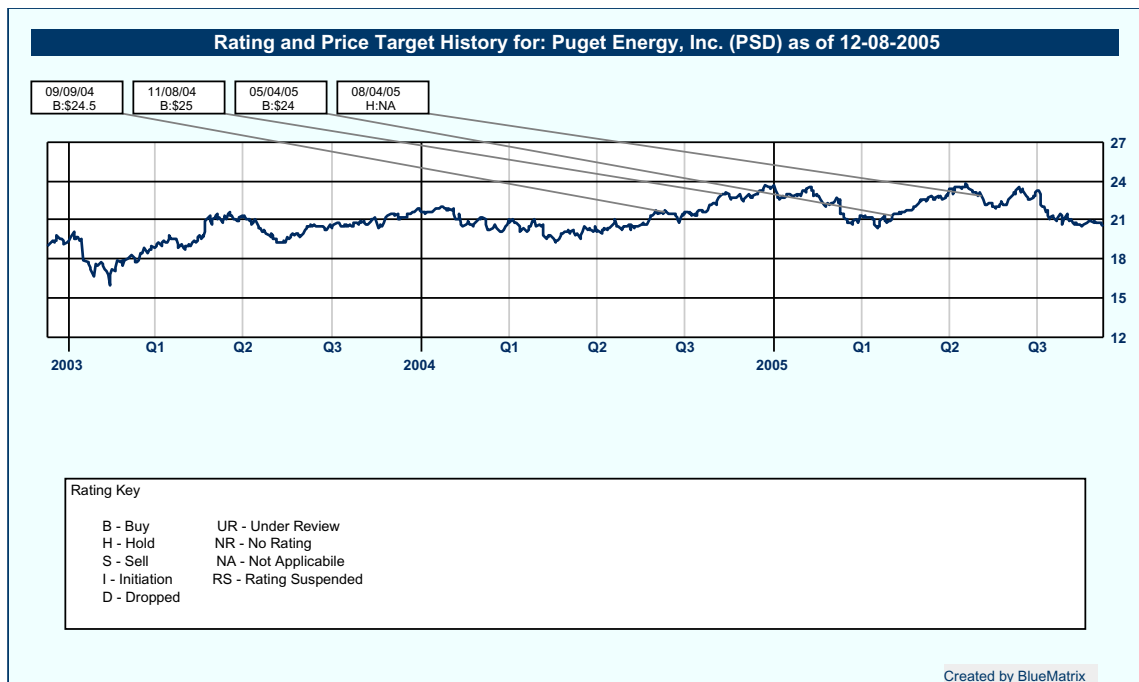
2004 Q2 Includes \$0.28 charge related to Tenaska order  
 2004 Q4 Includes \$0.77 charge related to goodwill impairment

Revenue (Net)	\$2.20B	\$2.53B	\$2.73B
EV/Revenue	NM	NM	NM



### Important Disclosures and Certifications

I, Selman Akyol, certify that the views expressed in this research report accurately reflect my personal views about the subject securities or issuers; and I, Selman Akyol, certify that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendation or views contained in this research report.



For a price chart with our ratings and target price changes for PSD go to <http://sf.bluematrix.com/bluematrix/Disclosure?ticker=PSD>

Stifel, Nicolaus & Company, Inc. or an affiliate expects to receive or intends to seek compensation for investment banking services from Puget Energy, Inc. in the next 3 months.

Stifel, Nicolaus & Company, Inc.'s research analysts receive compensation that is based upon (among other factors) Stifel Nicolaus' overall investment banking revenues.

Our investment rating system is three tiered, defined as follows:

**BUY** -We expect this stock to outperform the S&P 500 by more than 10% over the next 12 months. For higher-yielding equities such as REITs and Utilities, we expect a total return in excess of 12% over the next 12 months.

**HOLD** -We expect this stock to perform within 10% (plus or minus) of the S&P 500 over the next 12 months. A Hold rating is also used for those higher-yielding securities where we are comfortable with the safety of the dividend, but believe that upside in the share price is limited.

**SELL** -We expect this stock to underperform the S&P 500 by more than 10% over the next 12 months and believe the stock could decline in value.

Of the securities we rate, 40% are rated Buy, 59% are rated Hold, and 1% are rated Sell.

Within the last 12 months, Stifel, Nicolaus & Company, Inc. or the prior owner of part of the Stifel Nicolaus Capital Markets business has provided investment banking services for 31%, 27% and 33% of the companies whose shares are rated Buy, Hold and Sell, respectively.

We also use a Risk rating for each security. The Risk ratings are Low - 1, Average - 2, and High - 3 and are based primarily on the strength of the balance sheet and the predictability of earnings.

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January 10, 2006

**PUGET ENERGY, INC.**

PSD – NYSE

**Rating:**  
**BUY ↑****Price:** (1/10/05) \$20.78**Price Targets:**

12-18 month: \$23.50 ↑

5-year: \$30

**Industry:**

Utilities

**James L. Bellessa, Jr., CFA**

406.791.7230

jbellessa@dadco.com

FY (Dec)	2004A <sup>1</sup>	2005E <sup>2</sup>	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,198.9	\$2,523.4	15%	\$2,637.2	5%
Previous	-	NC		\$2,602.6	
Price/Revenue ratio	.9x	.9x		.9x	
<b>EPS Revised</b>	<b>\$1.26</b>	<b>\$1.40</b>	11%	<b>\$1.45</b>	4%
Previous	-	\$1.39		\$1.43	
Price/EPS ratio	16.6x	14.9x		14.3x	
<b>EBITDA (\$M)</b>	\$597.4	\$642.3	8%	\$714.6	11%
EV/EBITDA ratio	7.8x	7.2x		6.5x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05A	<b>\$0.72</b>	-	\$741.7	-	\$215.9
6/30/05A	<b>\$0.12</b>	-	\$510.1	-	\$119.3
9/30/05A	<b>\$0.06</b>	-	\$490.4	-	\$112.0
12/31/05E	<b>\$0.49</b>	\$0.48	\$781.3	NC	\$195.2

EPS represents results from continuing operations. <sup>1,2</sup>See detail of footnotes on page 2.**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (9/30/05)	60.7%
Cash per share (9/30/05)	\$0.11
Book value per share (9/30/05)	\$16.61
Dividend (yield)	\$1.00 (4.8%)
Return on Equity (T-T-M)	5%

**Trading Data**

Shares outstanding (M)	100.5
Market Capitalization (\$M)	\$2,088
52-week range	\$20.21 - \$24.37
Average daily volume (3 mos.) (K)	422
Float	99%
Index Membership	S&P 400 MidCap

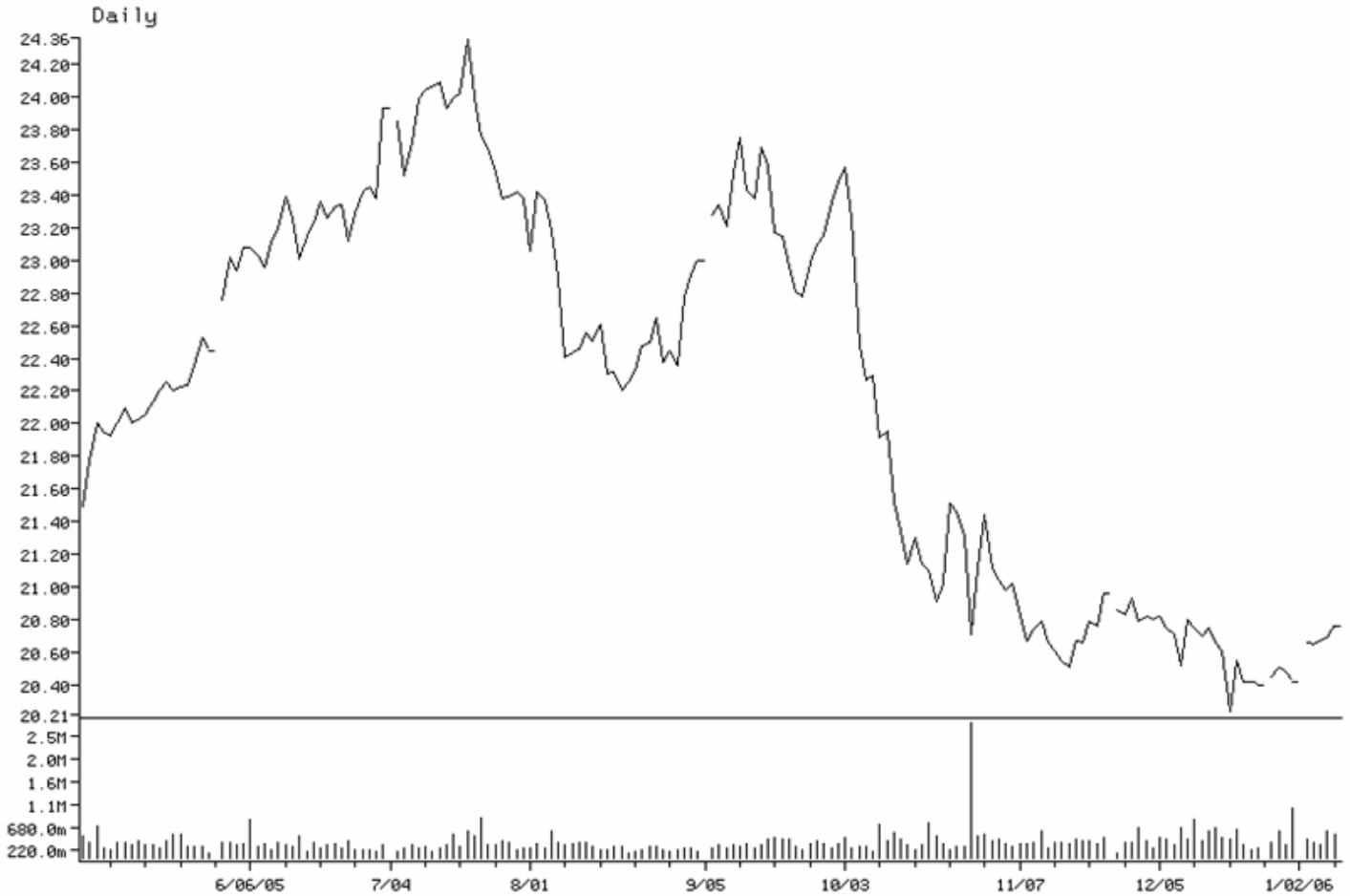
**Raising Estimates and Target Price. Upgrading to BUY.****Initiating Quarterly 2006 EPS Estimates and a 2007 Forecast.**

- As shown above, we are slightly raising our 2005 and 2006 EPS estimates from continuing operations because the underwriter's over allotment, which we were previously assuming, was not exercised following a recent share offering.
- We are forecasting 4Q'05 EPS of \$0.49, which compares to \$0.59 a year ago, when tax changes added \$0.05 per share to the quarter, and management's inferred quarterly guidance range of \$0.40-\$0.50.
- We believe that 4Q'05 results will be helped by slightly colder weather, and March and November rate increases. Offsetting these benefits should be a lack of last year's tax benefits, higher depreciation and amortization expenses, and increased shares due to the late October offering of 15 million shares.
- As shown in our earnings model, we are initiating quarterly EPS estimates for 2006. We are also initiating a 2007 EPS forecast of \$1.57.
- A year ago, the company announced it would divest its utilities construction business, InfrastruX, and in the interim period would account for it in discontinued operations. We believe an announcement of the divestiture should soon be forthcoming, with the proceeds being used to fund utility capital projects.
- We are raising our target price by a half point to \$23.50, or 15.5x the average of our 2006 and 2007 EPS estimates. With ample enough total return prospects, including a current dividend yield of 4.8%, we are raising our rating from NEUTRAL to **BUY**.

**Company Description:**

Belleve, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

<sup>1</sup>2004 data includes an after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

<sup>2</sup>2005 data includes 1Q'05 benefit of \$0.04/sh. for partial recovery of a previously reported regulatory disallowance related to the Tenaska gas supply regulatory asset and on-going disallowance of approximately \$0.02/sh. Includes 2Q'05 charges of \$0.02/sh for regulatory Tenaska disallowance and \$0.03/sh. for the true-up of previously reported gas costs.

2004 and 2005 data excludes results from discontinued operations, including (\$0.70) in 2004, (\$0.01) in 1Q'05, \$0.02 in 2Q'05.

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

	2000	2001	2002	2003	2004	9/30/2005A
<b>Assets</b>						
<b>Utility Plant:</b>						
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,389,882	\$4,645,289
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,881,768	1,966,806
Common plant	351,051	362,670	378,844	390,622	409,677	436,822
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,452,969)	(2,566,492)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,228,358	4,482,425
<b>Other Property and Investments:</b>						
Total other property and investments	292,297	317,249	378,130	402,093	157,670	157,249
<b>Current Assets:</b>						
Cash	36,383	92,356	176,669	27,481	12,955	9,817
Restricted cash			18,871	2,537	1,633	1,045
Accounts receivable, net						
Less: Allowance for doubtful accounts						
Total accounts receivable	343,108	279,321	279,623	227,115	137,659	112,283
Unbilled revenues	211,784	147,008	112,115	131,798	140,391	81,265
Inventories and supplies, at average cost	99,001	90,333	70,402	85,128	97,578	129,027
Purchased gas receivable	96,050	37,228			19,088	37,508
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	14,791	203,419
Taxes receivable						
Prepayments and other	11,607	11,277	11,323	12,200	8,273	34,485
Current assets of discontinued operations					110,922	122,664
Total current assets	797,933	660,838	672,744	493,852	543,290	731,513
<b>Long-Term Assets:</b>						
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	127,252	135,194
PURPA buyout costs	243,071	244,635	243,584	227,753	211,241	196,188
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	21,315	38,956
Power cost adjustment mechanism				3,605		5,583
Other	177,609	239,941	269,876	315,739	401,795	383,662
Long-term assets of discontinued operations					160,298	161,753
Total Long-term assets	628,030	680,909	690,388	698,513	921,901	921,336
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,851,219</b>	<b>\$6,292,523</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>						
Common stock	\$859,038	\$870	\$936	\$991	\$999	\$1,005
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,621,756	1,634,600
Earnings reinvested in the business	92,673	32,229	36,396	58,217	13,853	29,679
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(14,332)	3,266
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,622,276	\$1,668,550
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250	237,750
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,069,360	2,068,360
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	3,973,775	3,976,549
Minority interest in equity of a consolidated subsidiary			10,629	11,689	4,648	6,151
<b>Current Liabilities:</b>						
Accounts payable	410,619	167,426	205,619	214,357	226,478	216,668
Short-term debt	378,316	348,577	47,295	13,893		223,871
Current maturities of long-term debt	19,000	119,523	73,206	246,829	31,000	46,000
Purchased gas liability	0	0	83,811	11,984		
Accrued expenses:						
Taxes	103,996	70,708	62,562	77,451	81,315	77,297
Salaries and wages	17,445	14,746	11,441	12,712	13,829	12,125
Interest	43,955	42,505	37,942	32,954	29,005	42,901
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	26,581	14,643
Tenaska disallowance reserve					3,156	0
Other	26,685	46,178	47,761	46,378	34,918	28,994
Current liabilities of discontinued operations					51,892	73,783
Total current liabilities	1,000,016	844,808	572,047	660,194	498,174	755,875
Deferred Income Taxes	608,185	605,315	730,675	755,235	795,291	760,382
Other Deferred Credits	132,869	196,339	267,458	340,893	395,236	620,525
Commitments and Contingencies	0	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	385	0
Long-term liabilities of discontinued operations					183,710	173,041
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,851,219</b>	<b>\$6,292,523</b>

**% of Capitalization**

Total debt and mandatory redemption preferred	64.7%	67.4%	62.3%	60.3%	59.5%	60.7%
Preferred stock	1.4%	1.4%	1.4%	0.0%	0.0%	0.0%
Common stock	<u>33.9%</u>	<u>31.2%</u>	<u>36.3%</u>	<u>39.7%</u>	<u>40.5%</u>	<u>39.3%</u>
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Shares outstanding (000's)	85,904	87,023	93,643	99,074	99,868	100,460
Book value per share	\$16.61	\$15.66	\$16.27	\$16.71	\$16.24	\$16.61
Book value per share for the utility			<b>\$15.23</b>	<b>\$15.70</b>	<b>\$15.95</b>	<b>\$16.29</b>

## PUGET ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)

	4Q04**	2004**	1Q05	2Q05	3Q05	4Q05E	2005E	1Q06E	2Q06E	3Q06E	4Q06E	2006E	2007E
OPERATING REVENUES:													
Electric	\$404,778	\$ 1,423,034	\$420,090	\$345,420	\$375,035	\$445,330	\$1,585,875	\$449,732	\$369,983	\$378,837	\$459,280	\$1,657,833	\$1,677,938
Gas	284,703	769,306	321,129	162,567	111,042	335,465	930,203	346,212	170,453	115,530	345,158	977,353	1,023,443
Other	<u>2,531</u>	<u>6,537</u>	<u>434</u>	<u>2,127</u>	<u>4,306</u>	<u>500</u>	<u>7,367</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>2,000</u>	<u>2,500</u>
Total operating revenues	<u>692,012</u>	<u>2,198,877</u>	<u>741,653</u>	<u>510,114</u>	<u>490,383</u>	<u>781,295</u>	<u>2,523,445</u>	<u>796,445</u>	<u>540,936</u>	<u>494,867</u>	<u>804,938</u>	<u>2,637,186</u>	<u>2,703,881</u>
OPERATING EXPENSES:													
Energy costs:													
Purchased electricity	205,764	723,567	208,178	178,943	200,861	234,912	822,894	211,374	183,142	182,221	234,233	810,969	820,512
Purchased gas	180,618	451,302	201,744	98,142	59,151	221,713	580,750	222,275	104,084	64,459	225,105	615,923	634,186
Electric generation fuel	20,640	80,772	20,448	12,894	21,058	26,720	81,120	24,735	14,799	20,836	27,557	87,927	89,266
Residential Exchange	(50,674)	(174,473)	(55,046)	(37,105)	(34,525)	(50,768)	(177,444)	(55,317)	(36,998)	(34,474)	(51,439)	(178,229)	(178,700)
Unrealized (gain)/loss on derivative instruments	516	(526)	509	(591)	477	0	395	0	0	0	0	0	0
Utility operations and maintenance	77,083	291,232	75,522	83,132	81,645	82,000	322,299	78,000	84,000	83,000	84,000	329,000	332,000
Other operations and maintenance	741	2,324	741	558	745	500	2,544	500	500	500	500	2,000	2,000
Depreciation and amortization	58,529	228,566	58,077	59,657	60,550	64,000	242,284	64,500	65,500	66,000	68,000	264,000	267,000
Merger and related costs/conservation amort.	4,942	22,688	5,162	5,951	5,633	5,500	22,246	5,500	5,500	5,500	5,500	22,000	22,000
Goodwill Impairment													
Taxes other than federal income taxes	59,575	208,990	69,700	50,521	44,784	66,000	231,005	71,000	52,000	46,000	66,000	235,000	240,000
Federal income taxes	<u>36,134</u>	<u>76,757</u>	<u>46,084</u>	<u>6,093</u>	<u>2,476</u>	<u>32,793</u>	<u>87,446</u>	<u>49,349</u>	<u>9,187</u>	<u>6,427</u>	<u>38,613</u>	<u>103,576</u>	<u>113,458</u>
Total operating expenses	593,868	1,911,199	631,119	458,195	442,855	683,370	2,215,539	671,916	481,714	440,468	698,069	2,292,167	2,341,722
OPERATING INCOME	98,144	287,678	110,534	51,919	47,528	97,925	307,906	124,529	59,222	54,399	106,870	345,019	362,159
OTHER INCOME	<u>2,392</u>	<u>4,362</u>	<u>1,164</u>	<u>1,598</u>	<u>1,422</u>	<u>500</u>	<u>4,684</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>2,000</u>	<u>2,500</u>
INCOME BEFORE INTEREST CHARGES	100,536	292,040	111,698	53,517	48,950	98,425	312,590	125,029	59,722	54,899	107,370	347,019	364,659
INTEREST CHARGES, net of AFUDC	41,574	166,539	39,582	41,527	43,015	44,000	168,124	44,250	44,500	44,000	44,000	176,750	178,000
Mandatorily redeemable securities interest	23	91	23	23	23	23	92	23	23	23	23	92	92
Preferred stock dividends of subsidiary	0	0	0	0	0	0	0	0	0	0	0	0	0
INCOME FROM CONTINUING OPERATIONS	58,939	125,410	72,093	11,967	5,912	54,402	144,374	80,756	15,199	10,876	63,347	170,177	186,567
Discontinued Operations:	<u>(74,626)</u>	<u>(70,388)</u>	<u>(1,018)</u>	<u>1,928</u>	<u>(1)</u>	<u>0</u>	<u>909</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
NET INCOME before effect of acct. change	(15,687)	55,022	71,075	13,895	5,911	54,402	145,283	80,756	15,199	10,876	63,347	170,177	186,567
FAS-133 transition adjustment loss (net of tax)		0											
INCOME FOR COMMON STOCK	(\$15,687)	\$55,022	\$71,075	\$13,895	\$5,911	\$54,402	\$145,283	\$80,756	\$15,199	\$10,876	\$63,347	\$170,177	\$186,567
DILUTED COMMON SHARES OUT. --WEIGHTED	99,765	99,911	100,446	100,690	100,964	111,264	103,341	116,564	116,864	117,164	117,464	117,014	118,514
INCOME FOR COMMON STOCK													
Utility	\$58,939	\$125,410	\$72,093	\$11,967	\$5,912	\$54,402	\$144,374	\$80,756	\$15,199	\$10,876	\$63,347	\$170,177	\$186,567
Discontinued Operations	(\$74,626)	(70,388)	(1,018)	\$1,928	(\$1)	\$0	909	\$0	\$0	\$0	\$0	0	0
Cumulative effect of accounting change	0	0	0	0	0	0	0	0	0	0	0	0	0
Total	(\$15,687)	\$55,022	\$71,075	\$13,895	\$5,911	\$54,402	\$145,283	\$80,756	\$15,199	\$10,876	\$63,347	\$170,177	\$186,567
EARNINGS PER COMMON SHARE													
Utility	\$0.59	\$1.26	\$0.72	\$0.12	\$0.06	\$0.49	\$1.40	\$0.69	\$0.13	\$0.09	\$0.54	\$1.45	\$1.57
Discontinued Operations	(\$0.75)	(\$0.70)	(\$0.01)	\$0.02	(\$0.00)	\$0.00	\$0.01	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Cumulative effect of accounting change	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
DILUTED EARNINGS PER SHARE	(\$0.16)	\$0.55	\$0.71	\$0.14	\$0.06	\$0.49	\$1.41	\$0.69	\$0.13	\$0.09	\$0.54	\$1.45	\$1.57

\* We have attempted to conform our earnings model for the company's 1Q'05 decision to sell InfrastruX and to classify this utilities service business as a discontinued operation. While management has not yet provided restated data for 4Q'04, we have attempted to adjust our earnings model (even though not all rows and columns add), and use the assumption that InfrastruX will be divested by 1/31/06. \*\*Discontinued operations include 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.

D.A. Davidson & Co.

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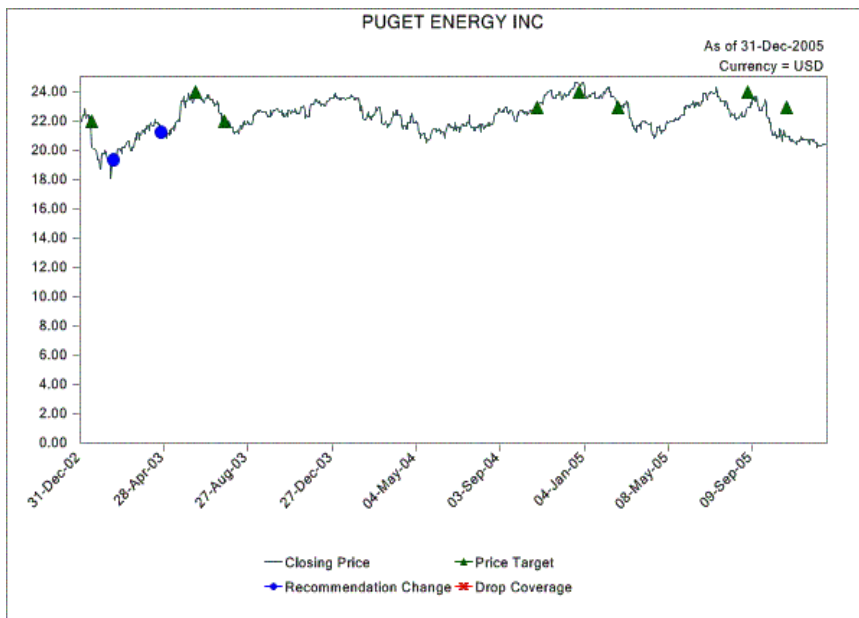
I, James L. Bellessa, Jr., CFA, attest that (i) all the views expressed in this research report accurately reflect my personal views about the common stock of the subject company, and (ii) no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

### Ratings Information

D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 12/31/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 40%	Neutral 50%	Underperform 10%
Corresponding Private Client Research Ratings and Distribution	Outperform 88%	Market Perform 12%	Underperform 0%
Distribution of Combined Ratings	48%	44%	8%

Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.	Buy	Hold	Sell
Institutional Coverage	8%	5%	6%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	6%	4%	6%



D.A. Davidson & Co. Institutional Research Rating Scale (maintained since 7/9/02)  
Buy, Neutral, Underperform

PUGET ENERGY INC					
Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	02-Nov-2005	21.03	23.00
14-Feb-2003	19.44	BUY	01-Sep-2005	22.90	24.00
			22-Feb-2005	22.88	23.00
			27-Dec-2004	24.62	24.00
			25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00

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Target prices are our Institutional Research Department's evaluation of price potential over the next 12-18 months and 5 years, based upon our assessment of future earnings and cash flow, comparable company valuations, growth prospects and other financial criteria. Certain risks may impede achievement of these price targets including, but not limited to, broader market and macroeconomic fluctuations and unforeseen changes in the subject company's fundamentals or business trends.

### **Other Disclosures**

Information contained herein has been obtained by sources we consider reliable, but is not guaranteed and we are not soliciting any action based upon it. Any opinions expressed are based on our interpretation of data available to us at the time of the original publication of the report. These opinions are subject to change at any time without notice. Investors must bear in mind that inherent in investments are the risks of fluctuating prices and the uncertainties of dividends, rates of return and yield. Investors should also remember that past performance is not necessarily an indicator of future performance and D.A. Davidson & Co. makes no guarantee, express or implied, as to future performance. Investors should note this report was prepared by D.A. Davidson & Co.'s Institutional Research Department for distribution to D.A. Davidson & Co.'s institutional investor clients and assumes a certain level of investment sophistication on the part of the recipient. Readers, who are not institutional investors or other market professionals, should seek the advice of their individual investment advisor for an explanation of this report's contents, and should always seek such advisor's advice before making any investment decisions. Further information and elaboration will be furnished upon request.

**Puget Energy, Inc.:**  
*PSD: Initiating Coverage with a HOLD Rating*

KeyBanc Capital Markets,  
 A Division of McDonald Investments Inc.

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**Investors should assume that we are seeking or will seek investment banking or other business relationships with the company described in this report.**

Rating	HOLD (3)
Price	\$20.69
12-Mo. Price Target	NA
Dividend	\$1.00
Yield	4.8%
52-Wk. Range	\$20-\$25
Trading Volume	NM
Market Cap. (mm)	\$2,389.7
Shares Out. (mm)	115.50
Book Value	\$16.61

Fiscal Year End	December
2006E	\$1.45
2005E	\$1.35
2004A	\$1.55
2006 P/E	14.3x
2005 P/E	15.3x
First Call 2006E	\$1.47
First Call 2005E	\$1.37

Next Quarter	December
Estimate	\$0.45
Vs.	\$0.59
First Call Estimate	\$0.49

**KEY INVESTMENT POINTS**

**We are initiating coverage of PSD with a HOLD (3) rating.** While the Company benefits from strong demographics with solid customer growth in an attractive region of the country, this proves to be a double-edged sword. The regulatory framework in Washington State precludes PSD from realizing the benefit of this growth on a timely basis. Because the state does not use forward-looking test years in rate cases, the utility faces a headwind recovering capital and cost increases between rate cases. This puts the Company in a position of being extremely challenged to earn its authorized return. It also necessitates the frequent filing of rate cases with accompanying regulatory uncertainty.

PSD's 2002 rate settlement alleviated much of the uncertainty that previously surrounded its net short power position in a region where power prices have been extremely volatile due to an interrelated dependency on hydroelectric output and purchased power. Under this regulatory framework, PSD has a mechanism where net power costs are shared between the customer and shareholder and costs above a baseline level are limited to \$40 million (plus 1% of costs above this threshold). This agreement is in place through June 30, 2006.

We look favorably on PSD's decision to divest its InfrastruX subsidiary. In our view, this simplifies the investment thesis for the shares, while eliminating the volatility surrounding the utility construction services industry, which is prone to the cyclicity of utility capital programs.

**We are initiating coverage with 2005 and 2006 estimates of \$1.35 and \$1.45, respectively.** These estimates reflect the negative impact of regulatory lag as the Company is pressured by continued operation and maintenance cost pressures as well as depreciation and amortization expenses above the level imbedded in base rates. We look for improved 2006 results from a full year of earnings from PSD's investment in a sizable (150 MW) wind farm which will be placed in rates through the power cost only rate case as well as a full year of higher rates from PSD's full gas and electric rate cases, which became effective in early March 2005. These items will be partly offset by dilution associated with the recent 15 million share equity offering.

**VALUATION**

Based upon our 2006 estimate, PSD shares sell at a modest discount to the peer (smaller vertically integrated) group average P/E ratio of 14.7x, compared to PSD's 14.3x. We believe this valuation is reasonable given the outlook for the continued inability to earn the authorized return and outlook for frequent rate cases.

**FOR IMPORTANT DISCLOSURES AND CERTIFICATIONS, PLEASE REFER TO PAGES 5 - 6 OF THIS NOTE.**

## **RISKS**

PSD is subject to several sources of risk in its business. As discussed, the Company must file frequent rate cases to minimize regulatory lag associated with inflation and capital spending. During a period of financial challenges related to the Western power crisis, the Commission authorized creative regulatory constructs allowing PSD the opportunity to rebuild its financial health. With the Company now on more solid ground, we have seen PSD's regulatory outcomes decreasingly allowing such opportunity.

Energy prices also could negatively impact PSD's results. While it is somewhat early to assess the actual impact that natural gas prices will have on demand levels, we believe customer conservation efforts could impact sales of natural gas and electricity. Further, even if prices were to retreat, some of these conservation habits may prove sticky.

Lastly is the sector specific risk that utility valuation levels return to a more historic discount to the broad market from current levels.

## **PSD AT A GLANCE**

PSD is the holding company of Puget Sound Energy. PSD is based in Bellevue, Washington, with Puget Sound Energy, its regulated gas and electric utility, operating mainly in the Puget Sound region of Washington. InfrastruX Group, the unregulated utility infrastructure construction and maintenance subsidiary operates in different regions nationwide. In February 2005, PSD announced its intention to divest InfrastruX, as the cyclical construction industry was not in tune with its desire for the stability offered by regulated utility operations. With a market capitalization of approximately \$2.4 billion, PSD is a smaller utility holding company. The Company generated nearly \$2.6 billion (nearly \$2.2 billion excluding InfrastruX) in revenues in 2004.

Following a period of financial difficulty related to poor conditions for PSD's hydroelectric plants and high unrecoverable electric energy costs, PSD has been improving its financial position to place the Company in a position to grow. The annual common stock dividend was cut from \$1.84 to \$1.00 per share. In 2001, with its net short power position, rate freeze (from a merger agreement) in place, the severe drought and rise in power prices, PSD's \$1.84 dividend was greater than its \$1.14 EPS. PSD has also shored up its balance sheet, which should help further stabilize its credit ratings. A constructive rate settlement agreement for its gas and electric business was also approved in 2002 for PSD, raising revenues and net income for both utility operations.

As part of the settlement agreement, the Washington Commission also granted Puget Sound Energy temporary rate relief to combat energy costs. A pass-through mechanism was introduced into customer billing so fluctuations in net power costs are reflected in rates and not entirely absorbed by the Company once a threshold has been crossed (which it has). As with its 2002 rate case, PSD has been permitting rates based upon a hypothetical equity ratio, to facilitate and expedite continued balance sheet improvement.

## **STRATEGY**

With the announced plans to divest the InfrastruX business, PSD is focused upon the core regulated utility operations. With the population drawing to the aesthetics of the Pacific Northwest, PSD enjoys strong customer growth with favorable demographics. Management seeks to lessen the impact of volatile pricing power by increasing physically owned generation. PSD foresees the need to add meaningful incremental capacity to decrease its net short power position. As demonstrated by PSD's ongoing addition of 380 MW of wind capacity, environmental factors drive management decision-making.

## **OVERVIEW OF BUSINESS SEGMENTS**

Puget Sound Energy (PSE) is PSD's regulated, gas and electric utility operation. Headquartered in Bellevue, Washington, Puget Sound Energy had at the end of 3Q05 1,013,739 electric customers and 683,404 gas customers, with over 300,000 who use it as both their gas and electric provider. Of the electric customers, approximately 894,929 are residential, 112,428 are commercial, 3,903 are industrial and 2,462 are other. The total number of electric customers grew by 23,500 in 2004, a growth rate of 2.4%. Although PSE's customer base is heavily residential, revenue is much more evenly spread out between residential and commercial. Residential revenue represented 47% of its billed electric revenue in 2004, while commercial represented 44%; industrial was 7% and 2% was other.

The 683,404 gas customers are comprised of approximately 629,963 residential, 50,637 commercial, 2,674 industrial and 130 transportation customers. PSE added 27,400 gas customers in 2004, which was a 4.3% increase. Its 2004 retail gas revenue was more residential-based, with 63% residential, 30% commercial, 5% industrial and 2% transport.

PSE's business is seasonal in that it is influenced heavily by weather. Winter weather affects the amount of gas and electricity used due to heating needs. Many heating systems in the Puget Sound region are older electrical resistance heaters rather than natural gas, creating higher electrical use during the winter. During the summer months, there is little air conditioning use in the Pacific Northwest. The first and fourth quarters of the calendar year tend to be PSE's most attractive for both gas and electric sales.



PSE currently purchases the majority of the electricity it supplies to its customers. In 2004, PSE supplied 31% of its total electric production through its own resources, 23% through long-term contracts with Washington Public Utility Districts, 19% from other firm purchases, and 27% from non-firm (spot) purchases. PSE's 1,963 MW of owned generation capacity is comprised of the Montana Colstrip plants (677 owned MW, coal fired), Baker River Hydro Project (180 MW), Snoqualmie Hydro Plant (42 MW), Electron Hydro Plant (22 MW), several dual-fuel (natural gas and petroleum fired) combustion turbines (791 MW), two natural gas fired plants (291 MW), an internal combustion plant (3 MW) and the newly completed Hopkins Ridge wind facility (150 MW). The Company plans to have a second 230 MW wind facility, Wild Horse completed by year-end 2006. While the total capacity of the wind projects is 380 MW, on average they are expected to generate 125 MW, due to variability of the wind resource.

The past few years have been marked by severe droughts in the Northwestern United States, which have hurt hydroelectric plants' energy outputs. The lack of power being produced by PSE's hydro plants forces the Company to purchase more power from outside sources. When there is enough water for the hydroelectric plants to produce excess power or market prices are above incremental cost of production or purchase, PSE sells power into the wholesale power markets.

PSE expects to see higher demands for power in its service territory in the near future. Economic factors have lowered industrial demands for power across the country, but PSD's service territory continues to see growth. Over the past 12 months, electric customer growth has been approximately 2% and the number of natural gas customers has grown at approximately 3% as PSD adds new customers and experiences electric to gas conversions. This growth is primarily in the residential and commercial sectors. PSD feels that customer growth will outpace its generation and supply capacity, and is formulating its plan to best meet the needs of its consumer base. PSD expects that through customer growth and contract expirations it will have a 305 MW generation capacity shortfall by the end of 2008, growing to 457 MW by the end of 2010. These amounts take into consideration the two wind capacity projects expected to be online by the end of 2006, with total capacity of 380 MW (125 MW on average, accounting for wind variability). PSD recently filed a Request for Proposals to address the forecast shortfall. The Company expects that it will rely on new purchase contracts and the purchase or construction of generation assets. Lately, PSD has focused on building its portfolio of owned assets. We view this favorably, as it provides longer-term growth through rate base additions and reduces exposure to volatile markets.

## **REGULATORY ISSUES**

PSD currently is operating under a Power Cost Adjustment mechanism, which limits its exposure to absorbing high purchased power costs. Specifics on the power cost adjustment pertain to the amount recoverable, when it is recoverable and what is taken into consideration for cost recovery. Through the plan, \$40 million of PSE's cumulative pretax earnings plus 1% of all other excess costs is at risk due to power cost variation. When the accumulated costs are \$40 million, excess costs are then split between shareholders (1%) and ratepayers (99%). This settlement is in effect until mid-2006. The specific factors being monitored when determining power cost variation are hydroelectric generation availability and variability, change in market price for purchased power, market price variability of surplus power sales, changes in natural gas and coal prices and plant outages. Special funds can be requested if during an actual or projected one-year period deferred power costs exceed \$30 million.

In October, 2003, Puget Sound Energy filed a power cost only rate case related to its proposed purchase of a 49.9% stake in the 249 MW combined cycle Frederickson plant. This acquisition is part of PSD's plan to increase its supply portfolio, with a bias toward owned generation, as opposed to contracted power purchases. In its initial filing PSD requested a \$64 million (4.72%) electric rate increase. Following intervenor testimony, PSD refiled for a \$54 million increase. In the WUTC staff recommendation, the acquisition and costs were deemed prudent. However, the staff also looked at the costs associated with two purchased power contracts the Company had entered into (Tenaska and Encogen). Puget Sound Energy had bought out the gas supply obligations related to these contracts during 1997 and 1999, respectively. At the time, orward gas markets suggested that fuel could be purchased more economically. Based upon expectations that PSE would purchase gas at costs lower than those in the contracts, the WUTC permitted the buyout premium to be collected from ratepayers.

As part of the Frederickson rate case, the WUTC ruled that PSE had not prudently contracted the required lower cost gas that would have produced the previously forecast savings and disallowed approximately \$10 million of PSE's \$54 million requested rate increase. Additionally, PSE was required to write-down an additional after-tax \$28.1 million related to these contracts. The WUTC noted that the actions deemed imprudent had occurred under a previous management structure. Because of the tenure of the contracts, PSD remains exposed to further prudence reviews. The Company has indicated that it expected from 2006 through 2008 disallowances to be \$8.8 million, \$7.7 million and \$6.3 million, respectively.

In April 2004, PSE filed a general rate case requesting electric and gas rate hikes of 5.7% and 6.3%, respectively. Aside from requesting to recover higher operating expenses and to earn on incremental infrastructure investment since its last rate case, PSE sought to change its allowed ROE and assumed capital structure. The rate filing requested an 11.75% ROE (from 11.0%) and a hypothetical equity ratio of 45% on a rate base of \$3.7 billion. In total, PSE requested to increase rates \$128.6 million, comprised of \$81.4 million electric and \$47.2 million on the gas side. Later in the case, PSE revised its requested electric increase to \$99.8 million.

On February 18, 2005, the WUTC issued an order authorizing a \$56.6 million electric rate increase and a \$26.3 million gas rate increase, effective March 4, 2005. These increases were premised upon a 10.3% ROE, a 43% equity ratio and a rate base of \$3.61 billion. The order also addresses PSD's request to limit exposure to catastrophic events by limiting this annual exposure to \$2.4 million, with deferral of the balance.

In October 2005, the WUTC approved a 3.7% (\$55.6 million) power cost only rate case related to the addition of the 150 MW Hopkins Ridge wind farm. New rates became effective November 1, 2005. The commission also requires PSD to file a general rate case by mid-February 2006, for new rates to become effective January 1, 2007. As part of the order, the WUTC modified to PCA mechanism by switching it over to a calendar year. The \$40 million limit to excess power costs expires June 30, 2006. Upon expiration of the cap, annual exposure to PSD shareholders/ratepayers follows: First \$20 million risk or benefit (PSD would benefit in a strong hydro or environment where power costs fell below baseline costs) borne 100%/0% by shareholder/ratepayer; \$20 million to \$40 million borne 50%/50%; \$40 million to \$120 million 10%/90% and over \$120 million 5%/95%, respectively. The recent ruling halved these amounts for the annualized July 1-December 31, 2006 period. In its next rate case, PSD will set to reset the baseline costs. We also expect the Company to propose changes to the PCA concept to reduce potential earnings volatility. While we would like to see forward-looking test years utilized in the state, we understand that this would likely require legislation.

In 2000, during very volatile western power pricing, PSD developed a plan to introduce time of use pricing to its customers. Through this innovative program, approximately 300,000 customers had real time meters installed. This plan was well received during the period of high priced power in the west, and PSD received kudos from many parties (including the White House). Since that time, prices have dropped, and the difference between on-peak and off-peak pricing has greatly diminished, making administrative costs outweigh the benefits derived. However, the program could be reactivated if volatility were to return.

### EARNINGS OUTLOOK

We are establishing initial 2005 and 2006 estimates of \$1.35 and \$1.45, respectively. As discussed, we expect WA regulation will preclude PSD from earning its authorized return given regulatory lag in a period of increased spending and personnel cost pressures. Hypothetically (with a 10.3% authorized ROE, 43% equity layer and rate base of \$3.61 billion), PSD could earn nearly \$160 million of net income or \$1.55 per share on a projected 2005 average share count of 103 million shares. However, several factors are expected to preclude this. Firstly, disallowances related to prudence reviews of Tenaska gas purchases are borne by shareholders. These costs are expected to be roughly \$10 million pre-tax or \$0.06-\$0.07 per share of net income. Inflationary pressures present a cost structure higher than that imbedded in rates by about \$0.05 per share. Lastly, capital spend due to strong customer growth in the region coupled with infrastructure spending to improve reliability do not get captured in rates until the next rate case is approved. This lag is expected to cause roughly \$0.10 of earnings drag.

For 2006, earnings should improve as the Hopkins Ridge wind farm presents greater rate base. The related \$55.6 million rate increase will be in place for an incremental 10 months in 2006. Additionally, PSD will pick up an incremental two months of the higher electric and gas base rates from the general rate case filed in 2004. This rate case yielded higher annual base rates of \$56.6 million and \$26.3 million at the electric and gas utilities, respectively. Tenaska disallowances should be of a similar or lesser magnitude. Offsetting these factors will be a full year of a higher share count (approximately 115 million vs. 103 million average shares outstanding).

PSD's \$1.00 per share annual dividend was premised upon a payout of 60% of normalized utility earnings. Given the level of capital spend over the coming few years, we would expect only modest, if any, dividend growth.

### EPS (Net) Summary

	2004A	%CHG	2005E	%CHG	2006E	%CHG
1Q	\$0.67	--	\$0.68A	1.5%	--	--
2Q	\$0.16	--	\$0.15A	-6.3%	--	--
3Q	\$0.13	--	\$0.06A	-53.8%	--	--
4Q	\$0.59	--	\$0.45	-23.7%	--	--
YEAR	\$1.55	--	\$1.35	-12.9%	\$1.45	7.4%

Source: McDonald Investments Inc. estimates

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We have managed or co-managed a public offering of equity securities for Puget Energy, Inc. within the past 12 months. Puget Energy, Inc. is an investment banking client of ours.

We have received compensation for investment banking services from Puget Energy, Inc. during the past 12 months

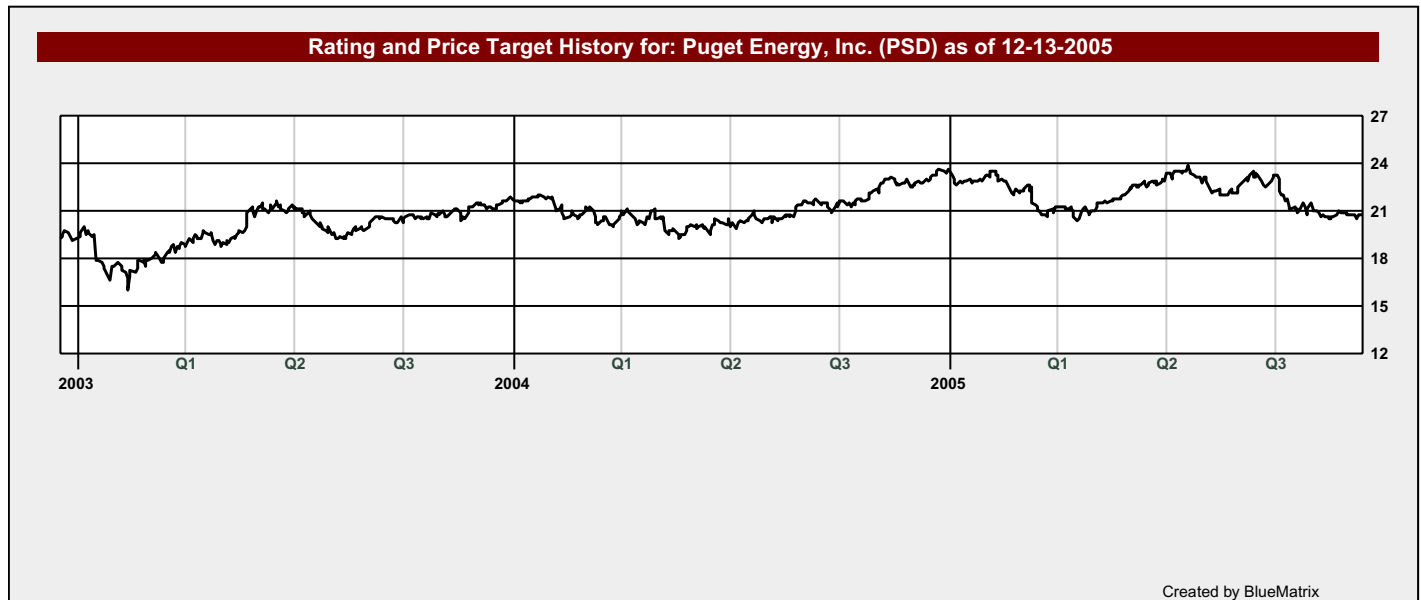
We expect to receive or intend to seek compensation for investment banking services from Puget Energy, Inc. within the next three months.

During the past 12 months, Puget Energy, Inc. has been a client of the firm or its affiliates for non-securities related services.

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### Three-Year Rating and Price Target History



### Rating Disclosures

Distribution of Ratings/IB Services Firmwide and by Sector									
KeyBanc Capital Markets			IB Serv./Past 12 Mos.		ENERGY				
Rating	Count	Percent	Count	Percent	Rating	Count	Percent	Count	Percent
BUY [AB/BUY]	187	45.50	49	26.20	BUY [AB/BUY]	31	41.89	17	54.84
HOLD [HOLD]	208	50.61	39	18.75	HOLD [HOLD]	43	58.11	18	41.86
SELL [UND/SELL]	16	3.89	3	18.75	SELL [UND/SELL]	0	0.00	0	0.00

### **Rating System**

AGGRESSIVE BUY (1) - The security is expected to outperform the market over the short term; investors should consider adding the security to their portfolios, subject to their overall diversification requirements.

BUY (2) - The security is expected to outperform the market over the long term; investors should consider adding the security to their holdings opportunistically, subject to their overall diversification requirements.

HOLD (3) - The security is expected to perform in line with general market indices; no buy or sell action is recommended at this time.

UNDERWEIGHT (4) - The security is expected to underperform the market; investors should reduce their holdings opportunistically.

SELL (5) - Absolute downside risk is evident for the security; investors should liquidate their holdings.

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# Investment Grade Research Company Update

December 15, 2005

Change in Recommendation

## Independent Power Producers & Utilities

### Puget Sound Energy, Inc.

[www.pse.com](http://www.pse.com)

NYSE: PSD

Selective Public Debt Issue as of December 15, 2005

Coupon %	Description	Maturity	Moody's/ S&P	Amount Outst. (\$mm)	Recent Price	YTW %	STW (bps)	Rec.
5.483	Secured	6/1/35	Baa2/BBB	\$250	\$96	5.76	102	HOLD

## Changing Bond Recommendation To HOLD

**Changing Recommendation Based on Relative Value.** We are downgrading our view on Puget Energy's (PSD's) subsidiary Puget Sound Energy's (PSE's) investment grade-rated first mortgage bonds (stable outlook) to HOLD from BUY in light of their strong bond performance relative to peers. Puget Sound Energy's bonds trade approximately 18 bps. tighter than Pacific Gas & Electric's 6.05% unsecured notes due 2034 and 28 bps. tighter than AEP subsidiary Appalachian Power's 5.95% unsecured notes due 2033. PSE's bonds have outperformed PG&E's and Appalachian Power's notes by roughly 10 bps since we initiated our BUY recommendation in July.

**Credit Profile Remains Strong.** LTM 3Q-05 EBITDA coverage of interest was approximately 4.5x, which we expect to strengthen modestly to 4.7x during 2006. Coupled with a debt to capital ratio of about 55%, we view PSD's credit profile to be a strong BBB. Financial performance is supported by a credit-conscious management team, who have shown a willingness to issue common stock to pay down debt and meet construction needs, as evidenced by issuance of 15 million common shares (proceeds of \$310 million) during October 2005.

**Regulatory Decisions Have Also Supported Current Ratings.** Recent Washington Commission decisions have supported the need for recovery of PSE's significant purchased power costs. In October, the Commission approved a settlement which allows PSE to recover \$55.6 million of purchased power costs beginning in November, including the costs associated with the new Hopkins Ridge wind farm. Puget Sound is also required to file a general rate case during mid-February 2006.

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**Third Quarter Update.** PSD reported 3Q-05 EBITDA of \$117 million, down from \$131 million during 3Q-04, reflecting higher planned plant outage and maintenance expenses which offset higher energy margins. PSD's 3Q-05 LTM EBITDA was \$760 million, up from \$743 million in FY-04 and the 3Q-05 LTM EBITDA coverage of interest ratio was a solid 4.5x times.

Balance sheet metrics and leverage statistics were strong at the end of the third quarter, and should be bolstered by common stock issuance that occurred early in 4Q-05. PSD's total debt to capital ratio and debt to EBITDA ratio were approximately 55% and 3.08x, respectively, at the end of the third quarter. PSD issued 15 million common shares during October 2005 to repay short-term debt incurred to fund a construction program.

**Pursuing Diversification to Offset High Natural Gas Costs.** PSE, which has historically purchased 70% of its power needs from third parties, is attempting to be more self-sufficient in energy generation resources. The acquisition of the 150 MW Hopkins Ridge wind project, which began operations during 4Q-05, along with construction of 230 MW Wild Horse wind project expected to be completed during 2006, should lessen the company's exposure to third-party power which is largely natural-gas fired. Following the Hopkins Ridge and Wild Horse additions, the utility would be short roughly 208 MW of capacity during 2006.

**Purchased power recovery.** On October 20, 2005, the Washington Commission approved a \$55.6 million (3.7%) annual increase in purchased power costs in a power cost only rate case (PCORC) following a settlement. Recovery of the newly-acquired Hopkins Ridge wind project was also included in the increase. The Commission also approved an amendment to the PCA mechanism by changing the annual PCA reporting periods to a calendar year period beginning January 1, 2007.

Under the current recovery plan, PSE is required to absorb a cumulative amount of excess purchased power costs of \$40 million plus 1% of the excess through June 30, 2006. Due to rapidly rising purchased power costs, the company has absorbed the initial \$40 million. In the October ruling, the Washington Commission approved a plan which limits PSE's exposure to \$10 million during the July 1, 2006 through December 31, 2006. The baseline purchased power cost recovery level is expected to be established prior to this six-month time frame.

Figure 1: Puget Summary Financials

HISTORICAL FINANCIAL INFORMATION	PROJECTIONS								
	3Q 04	4Q 04	1Q 05	2Q 05	3Q 05	YR 04	LTM	YR 05	YR 06
<b>Consolidated Financials</b>									
<i>Profitability/Cash Flow</i>									
<b>EBITDA</b>	\$ 131.2	\$ 299.8	\$ 220.4	\$ 123.0	\$ 116.7	\$ 743.1	\$ 759.9	\$ 753.1	\$ 797.1
Interest Expense	\$ (42.9)	\$ (43.5)	\$ (41.1)	\$ (41.5)	\$ (43.0)	\$ (173.1)	\$ (169.1)	\$ (162.0)	\$ (168.0)
Income Taxes	\$ (8.5)	\$ (30.7)	\$ (46.1)	\$ (6.1)	\$ (2.5)	\$ (75.0)	\$ (85.3)	\$ (74.0)	\$ (79.0)
Capital Expenditures	\$ (94.1)	\$ (96.7)	\$ (124.4)	\$ (97.0)	\$ (185.0)	\$ (434.3)	\$ (503.0)	\$ (600.0)	\$ (700.0)
Common Dividends	\$ (21.4)	\$ (21.8)	\$ (21.9)	\$ (22.0)	\$ (22.0)	\$ (86.9)	\$ (87.8)	\$ (88.0)	\$ (92.0)
<b>EBITDA less Op Costs &amp; Divs.</b>	\$ (35.7)	\$ 107.2	\$ (13.0)	\$ (43.6)	\$ (135.9)	\$ (26.1)	\$ (85.3)	\$ (170.9)	\$ (241.9)
<i>Credit Stats</i>									
EBITDA/Interest	3.06x	6.90x	5.37x	2.96x	2.71x	4.29x	4.49x	4.65x	4.74x
Debt/EBITDA	---	---	---	---	---	3.04x	3.08x		
Total Debt	\$ 2,332.9	\$ 2,259.8	\$ 2,197.4	\$ 2,310.0	\$ 2,338.2	\$ 2,259.8	\$ 2,338.2		
Total Preferred + TOPrs	\$ 282.1	\$ 282.1	\$ 282.1	\$ 239.6	\$ 239.6	\$ 282.1	\$ 239.6		
Total Common Equity	\$ 1,661.3	\$ 1,622.3	\$ 1,680.8	\$ 1,662.8	\$ 1,668.6	\$ 1,622.3	\$ 1,668.6		
Total Capital	\$ 4,276.3	\$ 4,164.2	\$ 4,160.3	\$ 4,212.4	\$ 4,246.4	\$ 4,164.2	\$ 4,246.4		
Debt/Capital	54.6%	54.3%	52.8%	54.8%	55.1%	54.3%	55.1%		
<b>OPERATING STATISTICS</b>									
<b>Electric Sales Statistics (mWhrs)</b>									
Total Retail Sales	4,462,421	5,461,887	5,630,327	4,573,063	4,530,700	19,884,193	20,195,977	20,083,035	20,283,865
Total Wholesale Sales	379,280	386,824	345,784	447,150	516,588	1,317,394	1,696,346	1,383,264	1,424,762
Total Energy Sales	4,841,701	5,848,711	5,976,111	5,020,213	5,047,288	21,201,587	21,892,323	21,466,299	21,708,627
Transportation	530,204	515,346	522,026	477,906	705,593	1,988,965	2,220,871	2,287,310	2,310,183
Energy Sales & Transportation	5,371,905	6,364,057	6,498,137	5,498,119	5,752,881	23,190,552	24,113,194	23,753,608	24,018,810
<b>Natural Gas Operating Statistics ('000 therms)</b>									
Natural gas sales to customers	87,676	276,540	308,203	142,145	90,353	808,558	817,241		
Transportation volumes	45,238	52,808	53,126	48,438	44,306	201,642	198,678		
Total gas volumes	132,914	329,348	361,329	190,583	134,659	1,010,200	1,015,919		
<b>REGULATORY HIGHLIGHTS</b>									
<b>Base Rates</b>	In February 2005, the Washington Commission authorized annual rate increases of \$56.6 million (4.5%) and \$26.3 million (3.5%) for PSE's electric and gas service respectively. The increases were premised upon a 10.3% ROE and an 8.4% overall return. PSE's rate base is comprised of \$2.5 billion in the electric division and \$1.1 billion in the gas division.								
<b>Purchased Power</b>	On Oct. 20, 2005, the Washington Commission approved a \$55.6 million (3.7%) increase in the recovery of purchased power costs in a power cost only rate case (PCORC). The new rates were effective Nov. 1, 2005 and include the recovery of costs associated with the Hopkins Ridge wind project. The order, which followed a settlement, also modified the Power Cost Adjustment rate mechanism.								

Source: Company Reports; Scotia Capital

## Scotia Capital (USA) Inc. (“SC-USA”)

Buy recommendation 29.5%  
Hold/Neutral recommendation 67.5%  
Sell recommendation 3%  
as of quarter ending September 30, 2005

### *Definition of Recommendations:*

- Buy:** The bond is projected to outperform the investment grade corporate bond market over the next 12 months.
- Hold:** The bond is projected to perform approximately in line with the investment grade corporate bond market over the next 12 month.
- Sell:** The bond is projected to underperform the investment grade corporate bond market over the next 12 months.

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- (ii) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this research report.



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Publication date: 30-Dec-2005  
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## Research Update: Puget Energy 'BBB-' Corp. Ratings Affirmed; Outlook Remains Stable

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Credit Rating:

BBB-/Stable/--

### Rationale

On Dec. 30, 2005, Standard & Poor's Ratings Services affirmed its 'BBB-' corporate credit ratings on Puget Energy Inc. (Puget) and subsidiary Puget Sound Energy Inc. (BBB-/Stable/A-3) The outlook is stable.

The ratings reflect the strong business profile of Puget Sound Energy, a regulated, vertically integrated electric and gas utility, and the consolidated financial risk profile of parent Puget. Puget's nonregulated construction subsidiary, InfrastruX (not rated), is not a primary credit factor, given Puget's plans to monetize the unit in 2006 and focus on Puget Sound Energy as its sole major subsidiary.

As of Sept. 30, 2005, Bellevue-based Puget had about \$2.3 billion in total debt, \$238 million in trust-preferred securities, and about \$121 million in guaranteed debt at InfrastruX.

Favorable developments in September 2005 and October 2005 provide further indication of the company's commitment to improve its credit position and of the Washington Utilities and Transportation Commission's (WUTC) support for recent resource acquisitions and the \$40 million power-cost cap, which expires on June 30, 2006. On Oct. 6, 2005, the WUTC granted in full the company's request for a 3.65% increase in electric rates and a 14% average increase in retail gas rates to support higher commodity costs and the addition of the 150 MW Hopkins Ridge wind project. In October 2005, Puget issued about \$310 million in common shares and applied the net proceeds to reducing short-term debt under its credit agreement.

Despite these achievements, Puget's credit outlook remains unchanged, primarily due to the company's dependence on a favorable outcome to the 2006 general rate case (GRC), which the WUTC has ordered by February 2006, as well as increased exposure to commodity cost volatility following the phase-out of the \$40 million power cost cap beginning on June 30, 2006.

Ratemaking by the WUTC remains the key driver of credit quality, especially in light of Puget Sound Energy's high capital needs and commodity price exposure.

While the WUTC has successively increased Puget Sound Energy's hypothetical equity layer, implemented a temporary \$40 million power cost cap, and fully supported capital cost recovery related to resource additions, a few of its decisions have impaired the company's ability to achieve its allowed ROE. After the power cost expires on June 30, 2006, the "sharing bands" of the power cost-adjustment mechanism will once again determine Puget Sound Energy's annual exposure to commodity cost volatility,

although the WUTC reduced these exposure levels by 50% for the last six months of 2006. The commission has ordered the company to file a general rate case by February 2006 to establish a new power cost baseline rate effective Jan. 1, 2007. The company's last general rate case resulted in a 10.3% ROE on a 43% hypothetical equity layer.

With the recent equity offering, cash flow coverage and debt leverage metrics are now within benchmark levels for the rating. Adjusted funds from operations (FFO) to interest coverage was 2.8x, while FFO to average total debt equaled 14% for the 12-month period ended Sept. 30, 2005. Adjusted debt leverage was 65% as of Sept. 30, 2005, but was subsequently reduced to about 61% with the application of about \$310 million in net proceeds from a October 26 common stock issuance to pay down short-term debt. Puget expects to internally fund about 50% of capital expenditures, with the balance funded with proceeds from equity and debt issuance.

### **Liquidity**

Overall liquidity at Puget was adequate, with credit event liquidity adequacy (CELA) and market and credit event liquidity adequacy (MCELA) ratios of 2x and 1.8x, respectively, as of Sept. 30, 2005, after adjusting for subsequent retirement of short-term debt in November 2005. As of Sept. 30, 2005, Puget Sound Energy had \$275.6 million in undrawn capacity under its \$500 million committed bank credit agreement that expires April 15, 2010. Secondary liquidity resources at Puget Sound Energy include an undrawn \$20 million uncommitted bank line and a \$150 million receivables securitization facility, through which \$70 million in receivables had been sold out of \$132 million in available receivables as of Sept. 30, 2005. On Sept. 29, 2005, Puget paid down the \$5 million drawn against its \$5 million committed credit agreement and retired the agreement.

Liquidity requirements will remain high at Puget Sound Energy in 2006 and 2007, due to about \$1.5 billion in planned capital spending and potential collateral requirements related to the company's electric and gas supply arrangements. Debt maturities are manageable, with about \$206 million in long-term debt due from 2006 to 2007, excluding the InfrastruX debt guaranteed as by Puget. Puget is the guarantor for up to \$150 million under a three-year credit agreement that expires in April 2007.

### **Outlook**

The stable outlook reflects Standard & Poor's expectation of reasonable rate relief for Puget Sound Energy, consistent with the WUTC's latest general rate case decision, offset by the phase-out of Puget Sound Energy's power cost cap in 2006. Credit stability will also depend not only on the approval of resource additions and sufficiency of rate relief, but also on maintaining a sufficient amount of equity to support capital investment needs and Puget Sound Energy's authorized 43% equity ratio. The outlook assumes that Puget will monetize in 2006 its unregulated subsidiary InfrastruX.

Consideration of a positive rating outlook will depend on more favorable rate relief in future years (beginning with the forthcoming GRC), consistently strong cash flow coverage metrics, and Puget Sound Energy's ability to improve its equity capitalization. An improved mechanism for commodity cost recovery could also provide support for a positive outlook. Alternatively, a negative outlook could result due to several factors, including additional commodity cost disallowances, the excessive accumulation of power cost deferrals, inadequate regulatory treatment of capital additions, a disproportionate reliance on debt financing to meet its capital needs, or significant power cost deficits beginning in 2007.

## Ratings List

Ratings Affirmed  
Puget Energy Inc.

Corp. credit rating            BBB-/Stable/--  
Puget Sound Energy Inc.

Corp. credit rating            BBB-/Stable/A-3

Senior secured debt            BBB

Preferred stock                BB

Complete ratings information is available to subscribers of RatingsDirect, Standard & Poor's Web-based credit analysis system, at [www.ratingsdirect.com](http://www.ratingsdirect.com). All ratings affected by this rating action can be found on Standard & Poor's public Web site at [www.standardandpoors.com](http://www.standardandpoors.com); under Credit Ratings in the left navigation bar, select Find a Rating, then Credit Ratings Search.

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**The McGraw-Hill Companies**

January 10, 2006

**PUGET ENERGY, INC.**

PSD – NYSE

**Rating:**  
**BUY ↑****Price:** (1/10/05) \$20.78**Price Targets:**

12-18 month: \$23.50 ↑

5-year: \$30

**Industry:**  
Utilities**James L. Bellessa, Jr., CFA**

406.791.7230

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FY (Dec)	2004A <sup>1</sup>	2005E <sup>2</sup>	Y-O-Y Growth	2006E	Y-O-Y Growth
<b>Revenue (\$M)</b>	\$2,198.9	\$2,523.4	15%	\$2,637.2	5%
Previous	-	NC		\$2,602.6	
Price/Revenue ratio	.9x	.9x		.9x	
<b>EPS Revised</b>	<b>\$1.26</b>	<b>\$1.40</b>	11%	<b>\$1.45</b>	4%
Previous	-	\$1.39		\$1.43	
Price/EPS ratio	16.6x	14.9x		14.3x	
<b>EBITDA (\$M)</b>	\$597.4	\$642.3	8%	\$714.6	11%
EV/EBITDA ratio	7.8x	7.2x		6.5x	

<b>Quarterly Data:</b>	EPS	EPS Previous	Revenue (\$M)	Revenue Previous	EBITDA (\$M)
3/31/05A	<b>\$0.72</b>	-	\$741.7	-	\$215.9
6/30/05A	<b>\$0.12</b>	-	\$510.1	-	\$119.3
9/30/05A	<b>\$0.06</b>	-	\$490.4	-	\$112.0
12/31/05E	<b>\$0.49</b>	\$0.48	\$781.3	NC	\$195.2

EPS represents results from continuing operations. <sup>1,2</sup>See detail of footnotes on page 2.**Valuation Data**

Long-term growth rate (E)	4%
Total Debt/Cap (9/30/05)	60.7%
Cash per share (9/30/05)	\$0.11
Book value per share (9/30/05)	\$16.61
Dividend (yield)	\$1.00 (4.8%)
Return on Equity (T-T-M)	5%

**Trading Data**

Shares outstanding (M)	100.5
Market Capitalization (\$M)	\$2,088
52-week range	\$20.21 - \$24.37
Average daily volume (3 mos.) (K)	422
Float	99%
Index Membership	S&P 400 MidCap

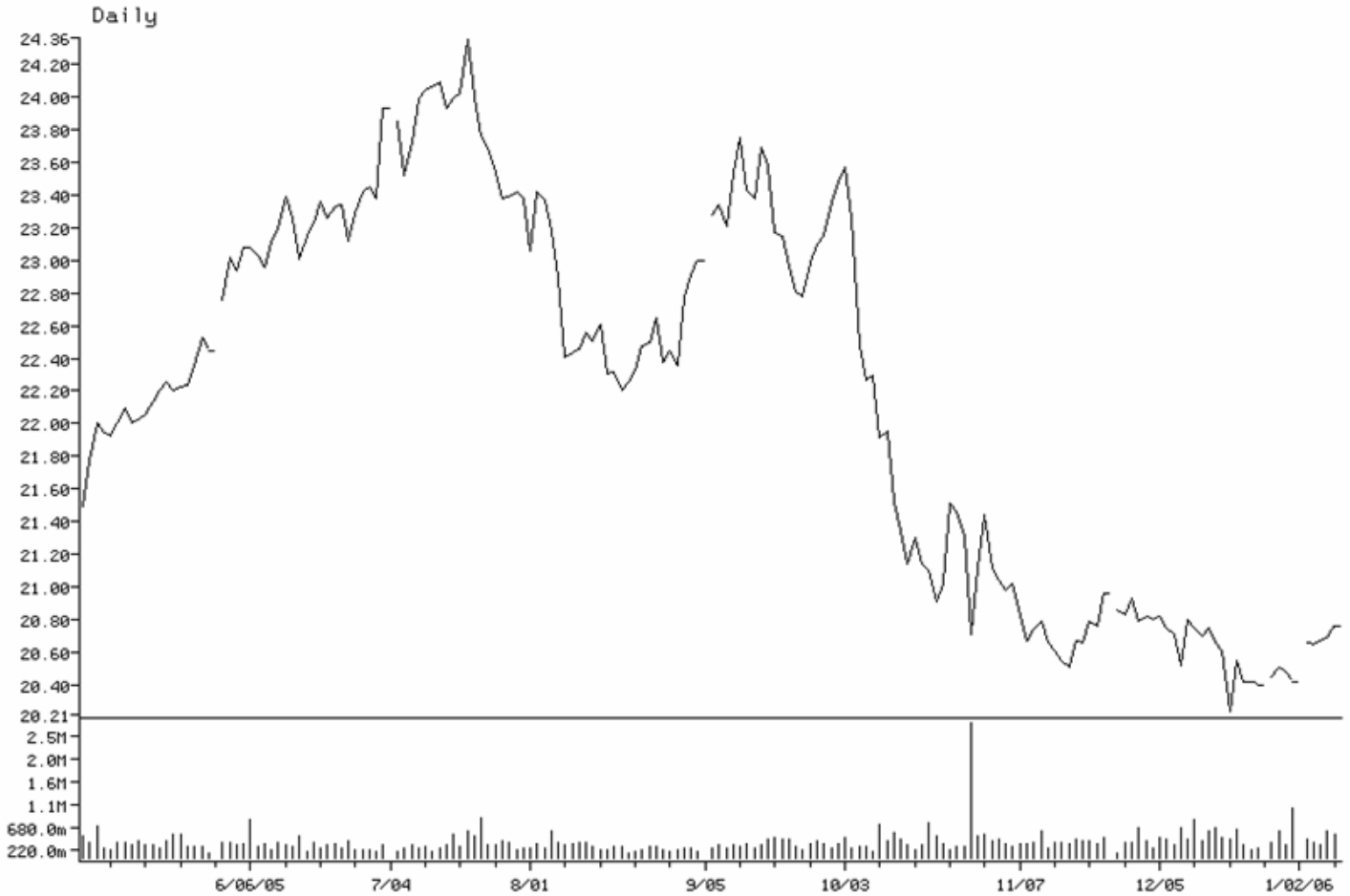
**Company Description:**

Bellevue, WA -- Puget Energy, Inc., through its wholly owned utility subsidiary, Puget Sound Energy, provides electric and gas services to more than 1.2 million customers, principally located in the Puget Sound region of Washington State. The firm has been focusing on low-risk energy distribution services, but has said it was seeking to return to a vertically integrated model. Puget has decided to exit the non-regulated utility services business called InfrastruX.

**Raising Estimates and Target Price. Upgrading to BUY.****Initiating Quarterly 2006 EPS Estimates and a 2007 Forecast.**

- As shown above, we are slightly raising our 2005 and 2006 EPS estimates from continuing operations because the underwriter's over allotment, which we were previously assuming, was not exercised following a recent share offering.
- We are forecasting 4Q'05 EPS of \$0.49, which compares to \$0.59 a year ago, when tax changes added \$0.05 per share to the quarter, and management's inferred quarterly guidance range of \$0.40-\$0.50.
- We believe that 4Q'05 results will be helped by slightly colder weather, and March and November rate increases. Offsetting these benefits should be a lack of last year's tax benefits, higher depreciation and amortization expenses, and increased shares due to the late October offering of 15 million shares.
- As shown in our earnings model, we are initiating quarterly EPS estimates for 2006. We are also initiating a 2007 EPS forecast of \$1.57.
- A year ago, the company announced it would divest its utilities construction business, InfrastruX, and in the interim period would account for it in discontinued operations. We believe an announcement of the divestiture should soon be forthcoming, with the proceeds being used to fund utility capital projects.
- We are raising our target price by a half point to \$23.50, or 15.5x the average of our 2006 and 2007 EPS estimates. With ample enough total return prospects, including a current dividend yield of 4.8%, we are raising our rating from NEUTRAL to **BUY**.

**Price Chart**



Source: ILX

**Footnote reference from page 1 of this report:**

<sup>1</sup>2004 data includes an after-tax charge of \$0.28/sh. for a regulatory disallowance of certain gas costs of the Tenaska generating plant, with \$0.25 falling in 2Q'04 and approximately \$0.02 falling in both 3Q'04 and 4Q'04. Includes a 4Q'04 goodwill impairment charge for InfrastruX of \$0.77/sh. after tax.

<sup>2</sup>2005 data includes 1Q'05 benefit of \$0.04/sh. for partial recovery of a previously reported regulatory disallowance related to the Tenaska gas supply regulatory asset and on-going disallowance of approximately \$0.02/sh. Includes 2Q'05 charges of \$0.02/sh for regulatory Tenaska disallowance and \$0.03/sh. for the true-up of previously reported gas costs.

2004 and 2005 data excludes results from discontinued operations, including (\$0.70) in 2004, (\$0.01) in 1Q'05, \$0.02 in 2Q'05.

**PUGET SOUND ENERGY, INC.****BALANCE SHEET**

(\$000's; years end 12/31)

	2000	2001	2002	2003	2004	9/30/2005A
<b>Assets</b>						
<b>Utility Plant:</b>						
Electric plant	\$4,054,551	\$4,167,920	\$4,229,352	\$4,265,908	\$4,389,882	\$4,645,289
Gas plant	1,459,488	1,551,439	1,645,865	1,749,102	1,881,768	1,966,806
Common plant	351,051	362,670	378,844	390,622	409,677	436,822
Less: Accumulated depreciation and amortization	(2,026,681)	(2,194,048)	(2,337,832)	(2,325,405)	(2,452,969)	(2,566,492)
Net utility plant	3,838,409	3,887,981	3,916,229	4,080,227	4,228,358	4,482,425
<b>Other Property and Investments:</b>						
Total other property and investments	292,297	317,249	378,130	402,093	157,670	157,249
<b>Current Assets:</b>						
Cash	36,383	92,356	176,669	27,481	12,955	9,817
Restricted cash			18,871	2,537	1,633	1,045
Accounts receivable, net						
Less: Allowance for doubtful accounts						
Total accounts receivable	343,108	279,321	279,623	227,115	137,659	112,283
Unbilled revenues	211,784	147,008	112,115	131,798	140,391	81,265
Inventories and supplies, at average cost	99,001	90,333	70,402	85,128	97,578	129,027
Purchased gas receivable	96,050	37,228			19,088	37,508
Current portion of FAS-133 unrealized gain (net of tax)		3,315	3,741	7,593	14,791	203,419
Taxes receivable						
Prepayments and other	11,607	11,277	11,323	12,200	8,273	34,485
Current assets of discontinued operations					110,922	122,664
Total current assets	797,933	660,838	672,744	493,852	543,290	731,513
<b>Long-Term Assets:</b>						
Regulatory asset for deferred income taxes	207,350	193,016	167,058	142,792	127,252	135,194
PURPA buyout costs	243,071	244,635	243,584	227,753	211,241	196,188
FAS-133 unrealized gain (net of tax)		3,317	9,870	8,624	21,315	38,956
Power cost adjustment mechanism				3,605		5,583
Other	177,609	239,941	269,876	315,739	401,795	383,662
Long-term assets of discontinued operations					160,298	161,753
Total Long-term assets	628,030	680,909	690,388	698,513	921,901	921,336
<b>Total Assets</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,851,219</b>	<b>\$6,292,523</b>

**Capitalization and Liabilities**

<b>Capitalization:</b>						
Common stock	\$859,038	\$870	\$936	\$991	\$999	\$1,005
Additional paid-in capital	470,179	1,358,946	1,484,615	1,603,901	1,621,756	1,634,600
Earnings reinvested in the business	92,673	32,229	36,396	58,217	13,853	29,679
Accumulated other comprehensive income	4,750	(29,321)	1,840	(8,063)	(14,332)	3,266
Total common equity	\$1,426,640	\$1,362,724	\$1,523,787	\$1,655,046	\$1,622,276	\$1,668,550
Preferred stock not subject to mandatory redemption	60,000	60,000	60,000	0	0	0
Preferred stock subject to mandatory redemption	58,162	50,662	43,162	1,889	1,889	1,889
Corporation obligated, mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the corporation	100,000	300,000	300,000	280,250	280,250	237,750
Long-term debt	2,170,797	2,127,054	2,149,733	1,969,489	2,069,360	2,068,360
Total capitalization	3,815,599	3,900,440	4,076,682	3,906,674	3,973,775	3,976,549
Minority interest in equity of a consolidated subsidiary			10,629	11,689	4,648	6,151
<b>Current Liabilities:</b>						
Accounts payable	410,619	167,426	205,619	214,357	226,478	216,668
Short-term debt	378,316	348,577	47,295	13,893		223,871
Current maturities of long-term debt	19,000	119,523	73,206	246,829	31,000	46,000
Purchased gas liability	0	0	83,811	11,984		
Accrued expenses:						
Taxes	103,996	70,708	62,562	77,451	81,315	77,297
Salaries and wages	17,445	14,746	11,441	12,712	13,829	12,125
Interest	43,955	42,505	37,942	32,954	29,005	42,901
Current portion of FAS-133 unrealized losses		35,145	2,410	3,636	26,581	14,643
Tenaska disallowance reserve					3,156	0
Other	26,685	46,178	47,761	46,378	34,918	28,994
Current liabilities of discontinued operations					51,892	73,783
Total current liabilities	1,000,016	844,808	572,047	660,194	498,174	755,875
Deferred Income Taxes	608,185	605,315	730,675	755,235	795,291	760,382
Other Deferred Credits	132,869	196,339	267,458	340,893	395,236	620,525
Commitments and Contingencies	0	0	0	0	0	0
Unrealized Loss on derivative instruments		75	0	0	385	0
Long-term liabilities of discontinued operations					183,710	173,041
<b>Total Capitalization and Liabilities</b>	<b>\$5,556,669</b>	<b>\$5,546,977</b>	<b>\$5,657,491</b>	<b>\$5,674,685</b>	<b>\$5,851,219</b>	<b>\$6,292,523</b>

**% of Capitalization**

Total debt and mandatory redemption preferred	64.7%	67.4%	62.3%	60.3%	59.5%	60.7%
Preferred stock	1.4%	1.4%	1.4%	0.0%	0.0%	0.0%
Common stock	<u>33.9%</u>	<u>31.2%</u>	<u>36.3%</u>	<u>39.7%</u>	<u>40.5%</u>	<u>39.3%</u>
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Shares outstanding (000's)	85,904	87,023	93,643	99,074	99,868	100,460
Book value per share	\$16.61	\$15.66	\$16.27	\$16.71	\$16.24	\$16.61
Book value per share for the utility			\$15.23	\$15.70	\$15.95	\$16.29

## PUGET ENERGY, INC. - CONSOLIDATED STATEMENTS OF INCOME\*

(000's, except per share; years end 12/31)	4Q04**	2004**	1Q05	2Q05	3Q05	4Q05E	2005E	1Q06E	2Q06E	3Q06E	4Q06E	2006E	2007E
<b>OPERATING REVENUES:</b>													
Electric	\$404,778	\$ 1,423,034	\$420,090	\$345,420	\$375,035	\$445,330	\$1,585,875	\$449,732	\$369,983	\$378,837	\$459,280	\$1,657,833	\$1,677,938
Gas	284,703	769,306	321,129	162,567	111,042	335,465	930,203	346,212	170,453	115,530	345,158	977,353	1,023,443
Other	<u>2,531</u>	<u>6,537</u>	<u>434</u>	<u>2,127</u>	<u>4,306</u>	<u>500</u>	<u>7,367</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>2,000</u>	<u>2,500</u>
Total operating revenues	<u>692,012</u>	<u>2,198,877</u>	<u>741,653</u>	<u>510,114</u>	<u>490,383</u>	<u>781,295</u>	<u>2,523,445</u>	<u>796,445</u>	<u>540,936</u>	<u>494,867</u>	<u>804,938</u>	<u>2,637,186</u>	<u>2,703,881</u>
<b>OPERATING EXPENSES:</b>													
Energy costs:													
Purchased electricity	205,764	723,567	208,178	178,943	200,861	234,912	822,894	211,374	183,142	182,221	234,233	810,969	820,512
Purchased gas	180,618	451,302	201,744	98,142	59,151	221,713	580,750	222,275	104,084	64,459	225,105	615,923	634,186
Electric generation fuel	20,640	80,772	20,448	12,894	21,058	26,720	81,120	24,735	14,799	20,836	27,557	87,927	89,266
Residential Exchange	(50,674)	(174,473)	(55,046)	(37,105)	(34,525)	(50,768)	(177,444)	(55,317)	(36,998)	(34,474)	(51,439)	(178,229)	(178,700)
Unrealized (gain)/loss on derivative instruments	516	(526)	509	(591)	477	0	395	0	0	0	0	0	0
Utility operations and maintenance	77,083	291,232	75,522	83,132	81,645	82,000	322,299	78,000	84,000	83,000	84,000	329,000	332,000
Other operations and maintenance	741	2,324	741	558	745	500	2,544	500	500	500	500	2,000	2,000
Depreciation and amortization	58,529	228,566	58,077	59,657	60,550	64,000	242,284	64,500	65,500	66,000	68,000	264,000	267,000
Merger and related costs/conservation amort.	4,942	22,688	5,162	5,951	5,633	5,500	22,246	5,500	5,500	5,500	5,500	22,000	22,000
Goodwill Impairment													
Taxes other than federal income taxes	59,575	208,990	69,700	50,521	44,784	66,000	231,005	71,000	52,000	46,000	66,000	235,000	240,000
Federal income taxes	<u>36,134</u>	<u>76,757</u>	<u>46,084</u>	<u>6,093</u>	<u>2,476</u>	<u>32,793</u>	<u>87,446</u>	<u>49,349</u>	<u>9,187</u>	<u>6,427</u>	<u>38,613</u>	<u>103,576</u>	<u>113,458</u>
Total operating expenses	593,868	1,911,199	631,119	458,195	442,855	683,370	2,215,539	671,916	481,714	440,468	698,069	2,292,167	2,341,722
<b>OPERATING INCOME</b>	<u>98,144</u>	<u>287,678</u>	<u>110,534</u>	<u>51,919</u>	<u>47,528</u>	<u>97,925</u>	<u>307,906</u>	<u>124,529</u>	<u>59,222</u>	<u>54,399</u>	<u>106,870</u>	<u>345,019</u>	<u>362,159</u>
<b>OTHER INCOME</b>	<u>2,392</u>	<u>4,362</u>	<u>1,164</u>	<u>1,598</u>	<u>1,422</u>	<u>500</u>	<u>4,684</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>500</u>	<u>2,000</u>	<u>2,500</u>
<b>INCOME BEFORE INTEREST CHARGES</b>	<u>100,536</u>	<u>292,040</u>	<u>111,698</u>	<u>53,517</u>	<u>48,950</u>	<u>98,425</u>	<u>312,590</u>	<u>125,029</u>	<u>59,722</u>	<u>54,899</u>	<u>107,370</u>	<u>347,019</u>	<u>364,659</u>
<b>INTEREST CHARGES, net of AFUDC</b>	<u>41,574</u>	<u>166,539</u>	<u>39,582</u>	<u>41,527</u>	<u>43,015</u>	<u>44,000</u>	<u>168,124</u>	<u>44,250</u>	<u>44,500</u>	<u>44,000</u>	<u>44,000</u>	<u>176,750</u>	<u>178,000</u>
Mandatorily redeemable securities interest	23	91	23	23	23	23	92	23	23	23	23	92	92
Preferred stock dividends of subsidiary	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>INCOME FROM CONTINUING OPERATIONS</b>	<u>58,939</u>	<u>125,410</u>	<u>72,093</u>	<u>11,967</u>	<u>5,912</u>	<u>54,402</u>	<u>144,374</u>	<u>80,756</u>	<u>15,199</u>	<u>10,876</u>	<u>63,347</u>	<u>170,177</u>	<u>186,567</u>
Discontinued Operations:	<u>(74,626)</u>	<u>(70,388)</u>	<u>(1,018)</u>	<u>1,928</u>	<u>(1)</u>	<u>0</u>	<u>909</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
<b>NET INCOME before effect of acct. change</b>	<u>(15,687)</u>	<u>55,022</u>	<u>71,075</u>	<u>13,895</u>	<u>5,911</u>	<u>54,402</u>	<u>145,283</u>	<u>80,756</u>	<u>15,199</u>	<u>10,876</u>	<u>63,347</u>	<u>170,177</u>	<u>186,567</u>
FAS-133 transition adjustment loss (net of tax)		0											
<b>INCOME FOR COMMON STOCK</b>	<u>(\$15,687)</u>	<u>\$55,022</u>	<u>\$71,075</u>	<u>\$13,895</u>	<u>\$5,911</u>	<u>\$54,402</u>	<u>\$145,283</u>	<u>\$80,756</u>	<u>\$15,199</u>	<u>\$10,876</u>	<u>\$63,347</u>	<u>\$170,177</u>	<u>\$186,567</u>
<b>DILUTED COMMON SHARES OUT. --WEIGHTED</b>	<u>99,765</u>	<u>99,911</u>	<u>100,446</u>	<u>100,690</u>	<u>100,964</u>	<u>111,264</u>	<u>103,341</u>	<u>116,564</u>	<u>116,864</u>	<u>117,164</u>	<u>117,464</u>	<u>117,014</u>	<u>118,514</u>
<b>INCOME FOR COMMON STOCK</b>													
Utility	\$58,939	\$125,410	\$72,093	\$11,967	\$5,912	\$54,402	\$144,374	\$80,756	\$15,199	\$10,876	\$63,347	\$170,177	\$186,567
Discontinued Operations	(\$74,626)	(70,388)	(1,018)	1,928	(\$1)	\$0	909	\$0	\$0	\$0	\$0	0	0
Cumulative effect of accounting change	0	0	0	0	0	0	0	0	0	0	0	0	0
Total	(\$15,687)	\$55,022	\$71,075	\$13,895	\$5,911	\$54,402	\$145,283	\$80,756	\$15,199	\$10,876	\$63,347	\$170,177	\$186,567
<b>EARNINGS PER COMMON SHARE</b>													
Utility	\$0.59	\$1.26	\$0.72	\$0.12	\$0.06	\$0.49	\$1.40	\$0.69	\$0.13	\$0.09	\$0.54	\$1.45	\$1.57
Discontinued Operations	(\$0.75)	(\$0.70)	(\$0.01)	\$0.02	(\$0.00)	\$0.00	\$0.01	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Cumulative effect of accounting change	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
<b>DILUTED EARNINGS PER SHARE</b>	<u>(\$0.16)</u>	<u>\$0.55</u>	<u>\$0.71</u>	<u>\$0.14</u>	<u>\$0.06</u>	<u>\$0.49</u>	<u>\$1.41</u>	<u>\$0.69</u>	<u>\$0.13</u>	<u>\$0.09</u>	<u>\$0.54</u>	<u>\$1.45</u>	<u>\$1.57</u>

\* We have attempted to conform our earnings model for the company's 1Q'05 decision to sell InfrastruX and to classify this utilities service business as a discontinued operation. While management has not yet provided restated data for 4Q'04, we have attempted to adjust our earnings model (even though not all rows and columns add), and use the assumption that InfrastruX will be divested by 1/31/06. \*\*Discontinued operations include 4Q'04 goodwill impairment charge for InfrastruX of \$76.6 million, or \$0.77/sh., after tax.



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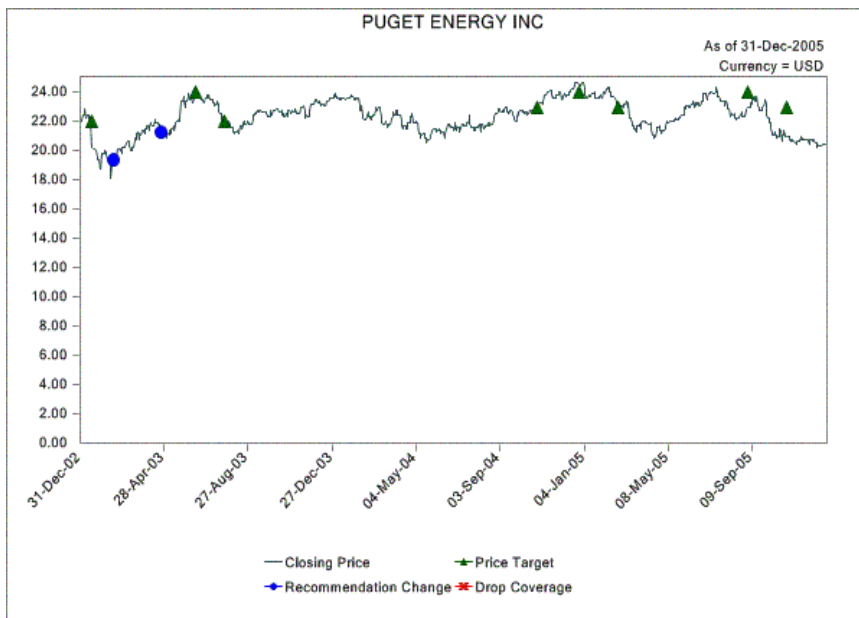
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D.A. Davidson & Co. Ratings	Buy	Neutral	Underperform
Risk adjusted return potential	Over 15% total return expected on a risk adjusted basis over next 12-18 months	>0-15% return potential on a risk adjusted basis over next 12-18 months	Likely to remain flat or lose value on a risk adjusted basis over next 12-18 months

Distribution of Ratings (as of 12/31/05)	Buy	Hold	Sell
Corresponding Institutional Research Ratings and Distribution	Buy 40%	Neutral 50%	Underperform 10%
Corresponding Private Client Research Ratings and Distribution	Outperform 88%	Market Perform 12%	Underperform 0%
Distribution of Combined Ratings	48%	44%	8%

Distribution of companies from whom D.A. Davidson & Co. has received compensation for investment banking services in last 12 mos.	Buy	Hold	Sell
Institutional Coverage	8%	5%	6%
Private Client Coverage	0%	0%	0%
Distribution of Combined Investment Banking	6%	4%	6%



D.A. Davidson & Co. Institutional Research Rating Scale (maintained since 7/9/02)  
Buy, Neutral, Underperform

PUGET ENERGY INC					
Currency = USD					
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
24-Apr-2003	21.35	NEUTRAL	02-Nov-2005	21.03	23.00
14-Feb-2003	19.44	BUY	01-Sep-2005	22.90	24.00
			22-Feb-2005	22.88	23.00
			27-Dec-2004	24.62	24.00
			25-Oct-2004	22.71	23.00
			24-Jul-2003	22.05	22.00
			12-Jun-2003	23.84	24.00
			16-Jan-2003	20.24	22.00

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