

**BEFORE THE STATE CORPORATION COMMISSION  
OF THE STATE OF KANSAS**

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**DIRECT TESTIMONY OF**

**MICHAEL W. CLINE**

**ON BEHALF OF  
KANSAS CITY POWER & LIGHT COMPANY**

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**IN THE MATTER OF THE PETITION OF  
KANSAS CITY POWER & LIGHT COMPANY (“KCP&L”)  
FOR DETERMINATION OF THE RATEMAKING PRINCIPLES  
AND TREATMENT THAT WILL APPLY TO THE RECOVERY  
IN RATES OF THE COST TO BE INCURRED BY KCP&L FOR  
CERTAIN ELECTRIC GENERATION FACILITIES  
UNDER K.S.A. 66-1239**

**DOCKET NO. 11-KCPE-581-PRE**

1 **Q: Please state your name and business address.**

2 A: My name is Michael W. Cline. My business address is 1200 Main Street, Kansas City,  
3 Missouri 64105.

4 **Q: By whom and in what capacity are you employed?**

5 A: I am employed by Great Plains Energy Services Incorporated, as Vice President -  
6 Investor Relations and Treasurer of Great Plains Energy Incorporated (“Great Plains  
7 Energy”), the parent company of Kansas City Power & Light Company (“KCP&L” or the

8 “Company”). References in my testimony to “the Companies” relate to Great Plains  
9 Energy and KCP&L.

10 **Q: What are your responsibilities?**

11 A: My responsibilities include financing and investing activities, cash management, bank  
12 relations, rating agency relations, financial risk management, investor relations, and  
13 acting as a witness with regard to financing and capital markets-related matters in the  
14 Company’s regulatory proceedings.

15 **Q: Please describe your education, experience and employment history.**

16 A: I graduated from Bradley University in 1983 with a B.S. in Finance, summa cum laude. I  
17 earned an MBA from Illinois State University in 1988. From 1984-1991, I was employed  
18 by Caterpillar Inc. in Peoria, Illinois and held a number of finance and treasury positions.  
19 From 1992-1993, I was Manager, International Treasury at Sara Lee Corporation in  
20 Chicago, Illinois. From 1994-2000, I was employed by Sprint Corporation in Overland  
21 Park, Kansas, initially as Manager, Financial Risk Management and then as Director,  
22 Capital Markets. During most of 2001, I was Assistant Treasurer, Corporate Finance, at  
23 Corning Incorporated in Corning, New York. I joined Great Plains Energy in October  
24 2001 as Director, Corporate Finance. I was promoted to Assistant Treasurer in  
25 November 2002. During 2004, I was assigned to lead the Company’s Sarbanes-Oxley  
26 Act compliance effort on a full-time basis, though I retained the Assistant Treasurer title  
27 during that time. I was promoted to Treasurer in April 2005 and added the title of Chief  
28 Risk Officer in July 2005. In February 2008, I was named Vice President-Investor  
29 Relations and Treasurer. I am also a Level II candidate for the Chartered Financial  
30 Analyst designation from the CFA Institute.

1 **Q: Have you previously testified in a proceeding at the Kansas Corporation**  
2 **Commission (“KCC” or “Commission”) or before any other utility regulatory**  
3 **agency?**

4 A: Yes, I have previously provided testimony to the KCC in the KCP&L Regulatory Plan,  
5 Docket No. 04-KCPE-1025-GIE (the “Regulatory Plan”); in KCP&L rate cases, Docket  
6 Nos. 06-KCPE-828-RTS, 07-KCPE-905-RTS, 09-KCPE-246-RTS, and 10-KCPE-415-  
7 RTS (the “415 Docket”); and in the Aquila acquisition case, Docket No. 07-KCPE-1064-  
8 ACQ. I have also testified before the Missouri Public Service Commission.

9 **Q: What is the purpose of your testimony?**

10 A: The purpose of my testimony is to explain (1) why the predetermination sought by the  
11 Company in this proceeding is important to the Company’s financial stakeholders, as  
12 well as (2) the implications such a determination has for the Company’s access to and  
13 cost of capital; and (3) to answer the following questions raised by the Commission in  
14 Docket No. 11-GIME-492-GIE (the “492 Docket”), paragraph 15, sections (b) and (c),  
15 specifically:

16 (b) If a utility is successful in a predetermination proceeding, then it has  
17 shifted some risk from its shareholders to its ratepayers. Should the utility’s stake  
18 in the generating facility, which was the subject of the predetermination  
19 proceeding, have different rate-making principles and treatment applied than  
20 would have been applied in a traditional rate case?

21 (c) Will pre-approval reduce the utility’s risk profile going forward? If so,  
22 should an adjustment be made to the utility’s return on equity in connection with  
23 whatever pre-approval is granted to the utility?

1 **Q: What type of determination is KCP&L requesting?**

2 A: The full scope of the Company's request, including the impact on customers, is described  
3 in the Direct Testimony of Company witness Chris Giles. In terms of my testimony, the  
4 two most relevant elements outlined by Mr. Giles include (a) a finding by the  
5 Commission that KCP&L's plan to install wet scrubbers, baghouses and a common  
6 chimney for La Cygne Units 1 and 2 and a Selective Catalytic Reduction system and low-  
7 nitrogen oxide burners for Unit 2 is prudent (decisional prudence); and (b) a finding by  
8 the Commission that the estimated cost to complete the project outlined in (a), up to  
9 \$1.23 billion on a total project basis is prudent (cost prudence) and that KCP&L's Kansas  
10 jurisdictional portion of those costs will be included in the Company's rates, by inclusion  
11 in rate base either in future rate proceedings or through a rider, with any amount in excess  
12 of the pre-approved amount subject to additional prudence review.

13 **Q: When you mentioned the Company's "financial stakeholders" earlier, to whom**  
14 **were you referring?**

15 A: The Company's "financial stakeholders" are parties in the financial community who have  
16 an interest in the Company's activities. These parties include current and prospective  
17 equity and fixed income investors, banks, and credit rating agencies.

18 **Q: Do your job responsibilities entail frequent contact with the Company's financial**  
19 **stakeholders?**

20 A: Yes. As the officer with primary responsibility for the Companies' investor relations and  
21 treasury functions, I correspond with current and prospective equity and fixed income  
22 investors and analysts, as well as banks, on virtually a daily basis. I also have primary

1 officer-level accountability for managing the Companies' relationships with the rating  
2 agencies and am in contact with them frequently as well.

3 **Q: Do you believe that your frequent contact with investors, analysts, rating agencies**  
4 **and banks ("financial stakeholders") allows you to reasonably assess how those**  
5 **parties might respond to a regulatory issue such as the subject of this docket?**

6 A: Yes. Given the importance of regulatory matters to our business model, they are the most  
7 frequent topic of discussion with financial stakeholders. This provides me with a very  
8 good perspective regarding how those parties would be expected to view a given  
9 regulatory outcome.

10 **Q: Are financial stakeholders aware that the Company is considering a significant**  
11 **environmental retrofit project at La Cygne?**

12 A: Yes. The Company's 10-K disclosure related to the potential need for additional  
13 investment at La Cygne to comply with Best Available Retrofit Technology standards  
14 dates back to 2006. Recently, with the conclusion of the Comprehensive Energy Plan  
15 ("CEP") marked by the completion of Iatan Unit 2, financial stakeholders have been  
16 becoming increasingly more interested in the Company's post-CEP capital expenditure  
17 and investment plans. The Company's projected capital expenditures included in its  
18 2009 10-K included amounts for Environmental of \$16.4 million, \$189.1 million, and  
19 \$189.9 million for 2010, 2011, and 2012, respectively (source: 2009 10-K, page 42).  
20 Though not specifically identified as such in the 10-K, these amounts represented the  
21 Company's best estimates at the time of cash outflows related to the La Cygne project  
22 described earlier (for only the three years indicated) and we have represented them  
23 accordingly in our discussions with financial stakeholders. Said another way, there is an

1 already robust and increasing familiarity on the part of the Company's financial  
2 stakeholders that environmental retrofits at La Cygne represent the Company's next  
3 significant single large-scale investment following the completion of the CEP.

4 **Q: Did the recent Commission order in KCP&L's rate case, the 415 Docket, contain**  
5 **any discussion that may influence investor expectations with respect to KCP&L's**  
6 **decision to pursue predetermination?**

7 A: Yes. The Commission's discussion of its rationale for denying the Environmental Cost  
8 Recovery Rider ("ECRR") requested by KCP&L expressly pointed to other avenues  
9 available to the Company in lieu of an ECRR:

10 Also, utilities can now use procedures provided for by statute to mitigate  
11 the need for an ECRR mechanism. Under the predetermination statute, a  
12 utility can gain assurance before construction that a generation project is  
13 needed and its costs are considered reasonable. (Source: Order:  
14 1) Addressing Prudence; 2) Approving Application, in Part; & 3) Ruling  
15 on Pending Requests, Case No. 10-KCPE-415-RTS, November 22, 2010,  
16 page 113).

17 **Q: How would financial stakeholders view the two determinations you mentioned?**

18 A: The La Cygne project is a significant investment for the Company. Investors, rating  
19 agencies, and other financial parties familiar with the utility industry understand very  
20 well the regulatory risk profile of a significant project like La Cygne. In addition to  
21 financial and operational risk, regulatory risk is significant under traditional ratemaking,  
22 where the assessment of decisional prudence and the prudence of costs incurred occurs  
23 only after significant funds have already been invested. However, because Kansas  
24 affords utilities the ability to seek environmental cost recovery riders and/or  
25 predetermination for environmental projects and the Commission has authorized these  
26 mechanisms in the past, financial stakeholders expect Kansas utilities to pursue one or  
27 both of the alternative courses of action for such investments. As indicated above,

1           though the Commission rejected KCP&L's request for an ECRR in the 415 Docket, it  
2           clearly pointed to predetermination as a viable alternative for KCP&L. As a result, in my  
3           opinion, financial stakeholders expect KCP&L to pursue and obtain the two  
4           predeterminations previously mentioned. The below excerpt from a recent report  
5           (attached as Schedule MWC2011-1) from one of the Wall Street investment banks that  
6           prepares and makes available to investors research on Great Plains Energy appears to  
7           capture this sentiment with respect to predetermination for KCP&L on the La Cygne  
8           project, particularly given the Commission's denial of the Company's requested ECRR in  
9           the 415 Docket. In my opinion, based on recent conversations, this view reasonably  
10          reflects that of other financial stakeholders as well with regard to predetermination:

11                   The KCC denied KCP&L's request for an environmental cost recovery  
12                   rider (ECRR) similar to the one utilized by Westar Energy, GXP's  
13                   neighboring utility in Kansas..... Hence, we believe the KCC decision  
14                   may limit GXP's ability to recover future environmental capex on a timely  
15                   basis, perpetuating the existing regulatory lag. KCP&L had proposed to  
16                   use the ECRR to recover capital expenditures associated with the  
17                   necessary environmental retrofits at the two LaCygne coal-fired units,  
18                   which are required to be implemented by 6/1/2015.... We note, however,  
19                   that KCP&L may negotiate a different recovery mechanism, *or use the*  
20                   *existing predetermination statute, which enables companies to obtain*  
21                   *regulatory pre-approval certifying prior to construction that a project is*  
22                   *needed and its estimated costs are reasonable.* (Emphasis added.)  
23                   (Source: JP Morgan Research Report on Great Plains Energy dated  
24                   December 14, 2010, p. 9)

25   **Q:   What do you think would be the impact of the two determinations on the**  
26   **Company's ability to acquire additional capital on reasonable terms?**

27   A:   As I indicated in my previous response, in my view, financial stakeholders expect  
28   KCP&L to seek and obtain these two determinations before proceeding with any  
29   significant project at La Cygne. Those expectations are reflected in the Company's  
30   current cost of and access to capital, both of which the Company view as reasonable.

1 **Q: What do you think would be the impact of KCP&L moving forward without the two**  
2 **determinations sought in this proceeding, *i.e.*, using a traditional ratemaking**  
3 **approach, on the Company’s ability to acquire additional capital on reasonable**  
4 **terms?**

5 A: I believe that such an action would be deemed imprudent by the Company’s financial  
6 stakeholders and adversely affect the Company’s ability to attract capital on reasonable  
7 terms. To understand this, one must view the impact of this project on financial  
8 stakeholders from an historical perspective. Prior to the surge in nuclear generation  
9 projects, utilities under “traditional regulation” determined the need for, type, fuel source,  
10 and size of new generation. The utilities raised the capital and constructed the project.  
11 Once the project was complete and deemed in-service to supply customers, the utility  
12 filed a rate case to include the cost of the generation plant in rates. Subsequent to the  
13 completion of a large number of nuclear generation plants, regulators in a number of  
14 instances disallowed costs, in some cases because a decision made perhaps as long as a  
15 decade earlier was deemed imprudent based on economics at the time of the disallowance  
16 ruling. Subsequent to the nuclear surge, and deregulation of generation in many states,  
17 utilities that announced plans to construct major plant additions or large scale  
18 environmental projects came under much more intense scrutiny and encountered more  
19 resistance from financial stakeholders. This is not a new development. KCP&L  
20 recognized this prior to pursuing its Comprehensive Energy Plan (“CEP”) in 2004.  
21 KCP&L knew that investor and rating agency confidence, particularly with regard to  
22 decisional prudence, would be critical to the Company’s ability to attract the necessary



1 capital to finance the program and, as a result, pursued the Regulatory Plan to implement  
2 the CEP.

3 **Q: How do you respond to the Commission’s question in the 492 docket, “If a utility is**  
4 **successful in a predetermination proceeding, then it has shifted some risk from its**  
5 **shareholders to its ratepayers. Should the utility’s stake in the generating facility,**  
6 **which was the subject of the predetermination proceeding, have different rate-**  
7 **making principles and treatment applied than would have been applied in a**  
8 **traditional rate case?”**

9 A: First, I do not agree with the premise that the risk has been shifted from shareholders to  
10 ratepayers. In a successful predetermination proceeding, an assessment of the “right” or  
11 “prudent” cost has been made. Delivering the project at the “prudent” price involves no  
12 incremental risk to the customer. In fact, I would argue that determining up-front what  
13 represents a prudent project cost reduces customer risk because any cost over that defined  
14 amount will be subject to additional Commission scrutiny prior to being included in rates.

15 Second, with regard to the Commission’s question, my response from a cost of  
16 capital perspective would be “no.” Financial stakeholders view KCP&L as one company  
17 when they make the decision to invest capital, provide liquidity, or assign a credit rating.  
18 Money is fungible; an investor or bank that provides funding to KCP&L finances the  
19 overall operation, not just a given facility or a given project on a stand-alone basis.  
20 KCP&L’s cost of capital should be determined on that basis—not on the basis of  
21 ratemaking principles for a specific project.

22 **Q: How do you respond to the Commission’s following questions in the 492 docket,**  
23 **“Will pre-approval reduce the utility’s risk profile going forward? If so, should an**

1           **adjustment be made to the utility’s return on equity in connection with whatever**  
2           **pre-approval is granted to the utility?”**

3    A:    Certainly the Company’s regulatory risk on the La Cygne project would be less with  
4           predetermination compared to the same project without the benefit of that mechanism.  
5           However, given the fact Westar has already been granted predetermination in two  
6           dockets (Docket No. 07-WSEE-616-PRE and No. 08-WSEE-309-PRE) and the  
7           Commission has pointed to predetermination as an alternative for KCP&L in the absence  
8           of an ECRR, financial stakeholders would not perceive KCP&L’s risk profile as  
9           improved if predetermination were granted. Rather, predetermination represents the  
10          “base case” and stakeholders would perceive KCP&L’s risk as much higher without  
11          predetermination.

12                 With regard to the second question (which implies a downward adjustment to  
13                 return on equity (“ROE”) if determinations are granted), my response is that such a  
14                 change would not be warranted. Investors’ *current* expectations support the *current* cost  
15                 of equity; therefore, KCP&L’s pursuit and successful use of a regulatory mechanism –  
16                 one that is both available and has previously been implemented in the state – to establish  
17                 definition with respect to decisional and cost prudence is assumed in the Company’s  
18                 existing cost of capital. Therefore, no downward adjustment to ROE should be made.

19    **Q:    How would predetermination impact the cost of long-term debt for the Company?**

20    A:    Because I believe that fixed income investors, like other financial stakeholders, expect  
21           KCP&L to obtain predetermination before moving forward with the La Cygne project, I  
22           would not expect the Company’s cost of long-term debt to change significantly if  
23           predetermination were granted, everything else equal. Again, it is important to recognize

1 the impact of not having a favorable decision on predetermination. If KCP&L were to be  
2 required to move forward with the La Cygne environmental retrofit project absent  
3 predetermination, KCP&L's cost of debt could rise markedly based on investor  
4 perceptions of increased risk for the project and a less supportive regulatory environment.  
5 This could occur even if the rating agencies do not downgrade KCP&L's credit rating.  
6 Given long-term debt issuance anticipated by the Company this year through 2012 of  
7 **\*\* [REDACTED] \*\***, the adverse impact on the Company and its customers could  
8 be significant.

9 **Q: Would you expect a similar dynamic to what you just described for long-term debt  
10 to apply to KCP&L's cost of short-term debt as well?**

11 A: Yes. KCP&L obtains its short-term funding through the daily issuance of commercial  
12 paper ("CP") to money market investors. The cost of CP is driven by investors' view of  
13 KCP&L's risk profile. To the extent that KCP&L were to undertake the La Cygne  
14 project having been unsuccessful in obtaining the ability to use an available regulatory  
15 tool that has been granted in the past to other utilities in the state, KCP&L's short-term  
16 debt cost would be expected to increase, all other things being equal.

17 **Q: Is the level of KCP&L's CP significant?**

18 A: It certainly can be. For 2009-2010, KCP&L's quarter-end CP balance averaged just  
19 under \$190 million, with a high of approximately \$300 million.

20 **Q: How do you think the credit rating agencies would respond if the Company  
21 successfully obtained the determinations it is requesting in this proceeding?**

22 A: Given the positive change in KCP&L's outlook from "Negative" to "Stable" announced  
23 by both Moody's Investor Service ("Moody's") and Standard & Poor's ("S&P") in

1 March and April 2010, respectively, as well as the expectations I have already described,  
2 I would not expect that success in this docket would result in any immediate impact to the  
3 credit ratings or outlooks of the Company. Though that may well be the case, the  
4 potential positive longer term credit implications for KCP&L should not be discounted.  
5 The Moody's framework for evaluating credit ratings of regulated utility companies  
6 ascribes 50 percent of the rating to the regulatory climate. S&P's assessment of the  
7 Business Risk Profile of a regulated utility is based heavily on the regulatory climate as  
8 well. As reflected in recent published reports, both agencies currently consider Kansas a  
9 constructive regulatory environment for utilities. Over time, a pattern of additional  
10 developments that serve to corroborate and strengthen that view could be beneficial  
11 longer-term to the credit profile of the Company and positively affect access to and cost  
12 of capital.

13 **Q: Please summarize the views you have expressed in your testimony.**

14 A: The La Cygne environmental project is a significant undertaking for KCP&L and  
15 represents a significant portion of the Company's anticipated capital expenditures over  
16 the next few years. KCP&L's financial stakeholders have been aware of the potential  
17 need for major environmental investment at La Cygne for nearly four years and, over the  
18 past several months, have been increasingly interested in additional details around the  
19 timing and amount of spending and prospective regulatory treatment of the project.  
20 There is precedent in the state for granting predetermination and the Commission's order  
21 in the 415 Docket pointed to predetermination as an avenue for KCP&L to pursue in the  
22 absence of an ECRR. I therefore believe that KCP&L's financial stakeholders expect the  
23 Company to pursue and successfully obtain the determinations requested by KCP&L in

1 this case, particularly with regard to decisional prudence and cost prudence, before  
2 proceeding with the La Cygne project. Given this expectation, I would not expect a  
3 significant change to cost of or access to capital if the determinations were authorized.  
4 The risk to KCP&L in terms of access to and cost of capital, however, is the negative  
5 financial stakeholder response anticipated if the Commission were to reject the  
6 Company's request, thereby forcing KCP&L to follow the higher-risk traditional  
7 ratemaking model if it were to go forward with this very significant investment. KCP&L  
8 had these same concerns when it formulated the CEP and therefore pursued the  
9 Regulatory Plan to mitigate them. In the current environment, a mechanism to resolve  
10 decisional prudence and cost prudence is already available and financial stakeholders  
11 expect KCP&L to be allowed to use it.

12 **Q: Does that conclude your testimony?**

13 **A: Yes.**

BEFORE THE STATE CORPORATION COMMISSION  
OF THE STATE OF KANSAS

In the Matter of the Petition of Kansas )  
City Power & Light Company ("KCP&L") )  
for Determination of the Ratemaking )  
Principles and Treatment that Will Apply ) Docket No. 11-KCPE-\_\_\_\_-PRE  
to the Recovery in Rates of the Cost to be )  
Incurred by KCP&L for Certain Electric )  
Generation Facilities Under K.S.A. 2003 )  
SUPP. 66-1239 )

AFFIDAVIT OF MICHAEL W. CLINE

STATE OF MISSOURI )  
 ) ss  
COUNTY OF JACKSON )

Michael W. Cline, being first duly sworn on his oath states:

1. My name is Michael W. Cline. I work in Kansas City, Missouri, and I am employed by Great Plains Energy, the parent company of Kansas City Power & Light Company as Vice President-Investor Relations and Treasurer.

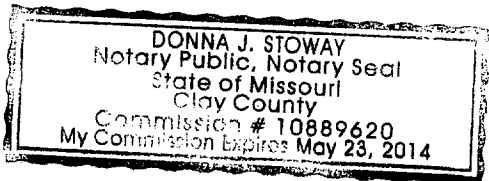
2. Attached hereto and made a part hereof for all purposes is my Direct Testimony on behalf of Kansas City Power & Light Company consisting of thirteen (13) pages, having been prepared in written form for introduction into evidence in the above-captioned docket.

3. I have knowledge of the matters set forth therein. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded, including any attachments thereof, are true and accurate to the best of my knowledge, information and belief.

Michael W. Cline  
Michael W. Cline

Subscribed and sworn before me this 12<sup>th</sup> day of February 2011.

[Signature]  
Notary Public



## Great Plains Energy

Assuming Coverage: We Remain on the Sidelines  
Until Regulatory Overhang Dissipates

We are assuming lead analyst coverage of Great Plains Energy and maintain our Neutral rating on the stock. GXP should benefit from earnings growth as the company reflects the final investments under its Comprehensive Energy Plan (CEP) in rates; however, we believe this is offset by the headline risk inherent in the pending rate cases in MO. As earnings visibility improves, we may be in a position to revisit our stance, but believe it is too early to do so yet. Accordingly, we maintain our Neutral rating on GXP shares.

- **Attractive rate base growth should boost the company's earnings power.** We expect recovery of capital investment under GXP's 5-year CEP to be the key driver of EPS growth in 2011 and 2012. The KS portion (~ 1/3 of the total capex) has already been reflected in rates, but the MO portion is still pending. We expect all CEP-related investments to be reflected in rates by mid-2011, and note that GXP's earnings power is predicated on constructive regulatory outcomes in the pending rate cases.
- **Lack of earnings visibility and headline risk in MO prompt us to remain on the sidelines.** Although GXP's pending rate cases in MO should boost its 2012 EPS, the regulatory uncertainty in a traditionally tough jurisdiction is a significant risk factor, in our view. Hence, we recommend that investors remain on the sidelines at least until the rate case hearings are completed, when visibility into the possible outcomes should improve.
- **Environmental retrofits likely to support long-term rate base growth.** Beyond the Comprehensive Energy Plan, we anticipate environmental retrofits at GXP's existing coal plants to constitute the most meaningful rate base growth driver going forward. Their timing and magnitude, as well as GXP's ability to negotiate appropriate regulatory treatment that minimizes regulatory lag, however, will likely determine the ultimate earnings impact.
- **Valuation appropriately balances EPS growth and residual risk.** Our Dec. 2011 price target of \$21 is based on a relative P/E valuation which reflects our updated earnings forecast. Despite their attractive growth prospects, we believe GXP shares should trade at a modest discount of ~ 5% vs. regulated peers in order to reflect the regulatory risk associated with the pending MO rate cases.

### Great Plains Energy, Inc. (GXP;GXP US)

	2009A	2010E (Old)	2010E (New)	2011E (Old)	2011E (New)	2012E
EPS Reported (\$)						
Q1 (Mar)	0.05	0.15A	0.15A			
Q2 (Jun)	0.28	0.47A	0.47A			
Q3 (Sep)	0.57	0.80A	0.96A			
Q4 (Dec)	0.10					
FY	1.03	1.45	1.60	1.70	1.60	1.65
Bloomberg EPS FY (\$)	1.16		1.55		1.57	1.75

Source: Company data, Bloomberg, J.P. Morgan estimates. Note: Official estimates rounded to the nearest \$0.05 per share. 'Bloomberg' above denotes Bloomberg consensus estimates.

## Neutral

GXP, GXP US

Price: \$19.27

▼ Price Target: \$21.00  
Previous: \$24.00

### Electric Utilities & IPPs

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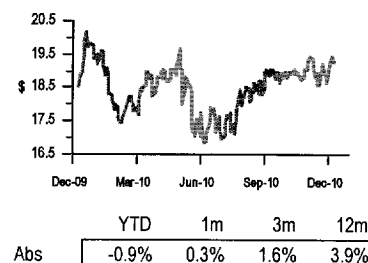
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J.P. Morgan Securities LLC

### Price Performance



### Company Data

Price (\$)	19.27
Date Of Price	10 Dec 10
52-week Range (\$)	20.29 - 16.63
Mkt Cap (\$ mn)	2,612.28
Fiscal Year End	Dec
Shares O/S (mn)	136
Price Target (\$)	21.00
Price Target End Date	31 Dec 11
Div. Yield	4.3%
Dividend (\$)	0.83

### See page 15 for analyst certification and important disclosures.

J.P. Morgan does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.

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## Table of Contents

<b>Key Investment Points</b> .....	<b>3</b>
<b>Investment Risks</b> .....	<b>4</b>
<b>Company Overview</b> .....	<b>6</b>
Investments Continue to Drive Rate Base Growth .....	6
One Rate Case Down in KS.....	8
... But Several More to Go Through in MO.....	9
Other Regulatory Concerns Expected to Persist .....	11
<b>Earnings and Cash Flow Analysis</b> .....	<b>12</b>
<b>Valuation and Rating Analysis</b> .....	<b>13</b>



## Key Investment Points

### Great Plains Energy (GXP)

Neutral

With three rate cases currently pending in MO, we anticipate the first half of 2011 to be a busy time for Great Plains Energy as the utilities seek to recover in rates the final capital expenditures related to Iatan 2. Although we expect rate case activity to ultimately boost the company's earnings power in 2011 and especially in 2012, we also anticipate disproportionate headline risk, which tempers our enthusiasm in the near term and forces us to remain on the sidelines.

#### **Recovering recent investments in rates should be the most immediate source of EPS growth**

Great Plains Energy is currently in the final stages of completing its Comprehensive Energy Plan (CEP), a 5-year investment program negotiated with regulators and stakeholders that committed the company to certain types of investments, including building the new supercritical coal-fired Iatan Unit 2. Recovering these investments in rates should boost GXP's earnings power in 2011 and 2012. The company just completed a rate case in KS with a reasonably constructive outcome, and is in the midst of a series of rate cases in MO to recover the MO jurisdictional portion of its spending. Achieving constructive regulatory outcomes in the pending rate cases would be a key determinant of GXP's near-term earnings power. Our estimates are premised on the company getting about half of its requested Missouri rate relief.

#### **Lack of earnings visibility and headline risk in MO remain key concerns for us**

Great Plains Energy's 2012 earnings power is predicated on three rate cases that are currently pending in Missouri, with hearings due in Jan.-Feb. 2011. Missouri regulation has traditionally been marked by contentious proceedings and below-average authorized returns. For example, Missouri Commission Staff recently recommended a 9% ROE in all pending cases, well below comparable returns in other jurisdictions. Thus, we perceive the hearings, as well as the final Commission rate orders, as a source of headline risk for the company, which tempers our enthusiasm in the next several months. Therefore, we recommend that investors remain on the sidelines at least until the hearings phase in the rate cases is completed and regulatory risk begins to dissipate.

#### **Environmental retrofits likely to drive rate base growth beyond 2011**

With the completion of the CEP this year, we anticipate environmental retrofits at GXP's existing coal plants to constitute the most meaningful rate base growth driver going forward. Although Great Plains has other investment options such as transmission and renewables projects, we believe they carry a higher hurdle rate and therefore are more uncertain in terms of magnitude and timing. While environmental capex could continue to drive attractive rate base growth in the near term, we believe its recovery is more uncertain than that of investments under the CEP. Consequently, negotiating the appropriate regulatory treatment that minimizes regulatory lag would be the key to translating rate base growth into earnings growth, in our view.

### **Expect the shares to trade sideways until regulatory risk dissipates**

Busy regulatory calendar in 1H11 likely to cause GXP shares to trade sideways. We continue to expect the company's busy regulatory calendar in 1Q11 and 2Q11 to cause the stock to trade sideways in the next several months as the regulatory overhang from several concurrent rate case proceedings in MO weighs on the stock.

### **Regulatory lag also continues to be a concern**

Since both Kansas and Missouri employ historical rate making, regulatory lag can be a significant concern. It has been mitigated in recent years by GXP's Energy Plan and the series of frequent rate cases that the plan contemplated. As the CEP comes to its logical end, however, regulatory lag remains a persistent concern for us, especially as the company embarks on a round of environmental retrofits over the next several years. We expect GXP management to work with regulators in both states to find ways to minimize regulatory lag going forward, although the actual means to do so remain uncertain.

### **Cost recovery trackers could be an effective way to mitigate regulatory lag**

As GXP contemplates additional environmental retrofits, we believe the use of cost recovery trackers, either for specific facilities or types of capex, would be an important tool to minimize regulatory lag. The company's Kansas regulators recently rejected GXP's proposed environmental cost recovery rider because they found it to be ill-suited for an investment as large as the LaCygne environmental retrofit, but did not preclude the company from seeking a modified environmental rider in the future.

### **Valuation appropriately reflects attractive growth prospects, balanced by residual regulatory overhang**

GXP shares trade at 12.1x our revised 2011E EPS of \$1.60 per share vs. a pure-play regulated peer group multiple of 13.9x. Although the stock appears to screen cheap relative to its regulated peers, we believe its valuation appropriately reflects GXP's attractive earnings growth prospects counterbalanced by the regulatory risk associated with the company's pending Missouri rate cases. As we obtain better visibility into GXP's 2011 and 2012 earnings power, we may revisit our investment thesis on the stock. In the meantime, however, we remain on the sidelines.

## Investment Risks

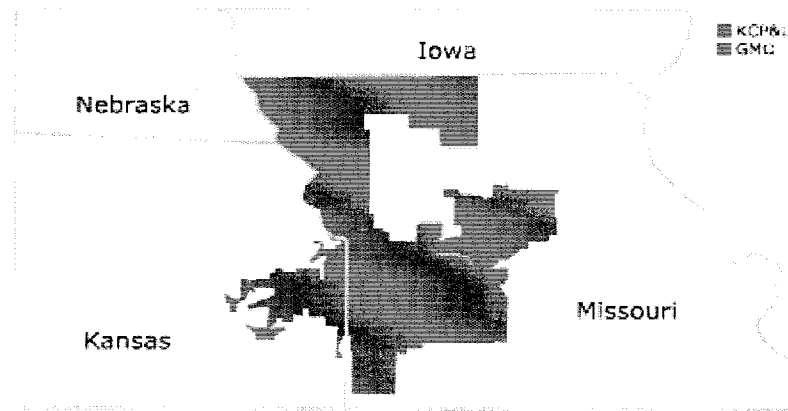
Our rating and price target could be at risk if:

- GXP's regulatory environment improves or deteriorates meaningfully.
- Great Plains has better investment opportunities than we project, or, conversely, some of its investments do not materialize.
- The company has to raise external equity financing in order to maintain its credit metrics or regulatory capital structure.
- GXP takes the dilution resulting from its equity units in mid-2012.
- Commodity prices fall sharply as Great Plains would not be able to earn the wholesale margin assumed in its rate structure.

### Company Description

Great Plains Energy (NYSE: GXP) is a vertically integrated electric utility serving over 820,000 customers in Missouri and Kansas. Headquartered in Kansas City, MO, the holding company operates through two principal subsidiaries: Kansas City Power & Light Company (KCP&L) with operations in KS and MO, and KCP&L Greater Missouri Operations Company (GMO) with operations in MO. GMO comprises of two separate legal entities, MPS and L&P, both of which were acquired by GXP from Aquila, Inc. on 7/14/2008. Neither Kansas nor Missouri have deregulated their electricity markets. Great Plains Energy is subject to regulation by the Missouri Public Service Commission (MPSC), the Kansas Corporation Commission (KCC), as well as by the Federal Energy Regulatory Commission (FERC) with respect to interstate transmission and wholesale electricity sales, and by the Southwest Power Pool (SPP) with respect to its transmission assets.

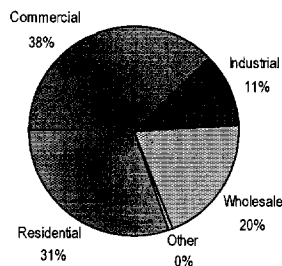
Figure 1: GXP Service Territory by Operating Segment



Source: Company reports.

## Company Overview

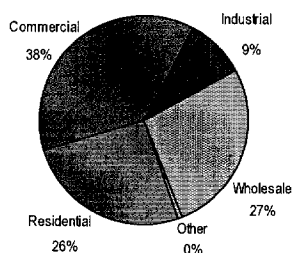
Figure 2: 2009 GXP Sales Breakdown



Source: Company reports and J.P. Morgan estimates.

Since the acquisition of Acquila, Inc.'s MO operations (now Greater Missouri Operations Company, or GMO) in July 2008 and the divestiture of its former unregulated subsidiary, Strategic Energy, in June 2008, Great Plains Energy has concentrated on its core electric utility operations and on regulated growth. At the same time, the legacy KCP&L segment remains focused on executing its 5-year Comprehensive Energy Plan (CEP), leading to above-average rate base growth in the past several years. Since Great Plains has largely completed the CEP, the key investor focus has shifted to recovering the last investments in rates. The company continues to experience meaningful regulatory lag in both of its jurisdictions, although the series of pending rate cases should cause the regulatory lag to diminish in the next 12 months, thus driving earnings growth. Beyond regulatory activity, we anticipate the integration of the GMO acquisition and resulting synergies to continue to support earnings growth as costs are squeezed out.

Figure 3: 2009 KCP&L Sales Breakdown



Source: Company reports and J.P. Morgan estimates.

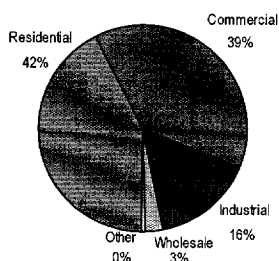
We expect the key near-term driver for GXP shares to be the busy regulatory calendar while the Missouri utilities complete the pending series of rate cases. In the meantime, we recommend that investors remain on the sidelines as we anticipate the regulatory overhang to cause GXP shares to trade sideways in the near term. As we obtain greater visibility into the magnitude of the earnings uplift and the company's earnings power in 2012 and beyond, we may revisit our investment thesis on the stock.

### Investments Continue to Drive Rate Base Growth

#### KCP&L's CEP drives meaningful rate base growth

In 2005, KCP&L embarked on an ambitious 5-year capital investment initiative, the Comprehensive Energy Plan (CEP), which is largely completed at this stage. By the end of 2010, we expect GXP's total rate base to reach about \$5.8 billion, up 60% from about \$3.6 billion at the end of 2008. Under this strategy negotiated with regulators and other stakeholders in Missouri and Kansas, KCP&L agreed to undertake a series of investments in five broad categories:

Figure 4: 2009 GMO Sales Breakdown



Source: Company reports and J.P. Morgan estimates.

**Environmental retrofits:** SCR at LaCygne Unit 1 (completed in 3Q06) and an air quality control system at Iatan Unit 1 (completed in 2Q09);

- ◆ **Construction of a new 850-MW supercritical coal unit**, Iatan 2 (in service at the end of Aug. 2010; total GXP share: 73%);
- ◆ **Wind generation investments:** 100 MW of wind capacity by 2010 (the Spearville Wind Energy Center; online in 3Q06), and up to an additional 300MW by 2012. GXP began construction of another 48 MW at the Spearville sit in 3Q10, which are expected to come online in December 2010.
- ◆ **Infrastructure improvement projects** focused on maintaining reliability and improving ageing and/or inadequate facilities;
- ◆ **Energy efficiency and demand response programs.**

Although the CEP does not equate to pre-approval, it significantly diminishes the risk of regulatory disallowances given that the regulators at least agreed on the types

**The CEP dramatically reduces regulatory risk, in our view.**

of capital investment projects that the utility should undertake included as part of the plan. Regulators, can, however, challenge the cost of individual projects. We note that there were no regulatory disallowances for GXP's investments in the Spearville wind farm, the environmental retrofit of LaCygne, and for Iatan 1 in the 2009 rate cases, and the regulatory disallowances for Iatan Unit 2 adopted in KCP&L's recent KS rate case have been relatively small. Hence, the CEP limits the potential liability that GXP may be exposed to and results in constructive regulatory treatment for the utility.

**Iatan Unit 2 ownership:**

**55% KCP&L  
18% GMO  
12% Empire District (EDE)  
15% munis & coops**

**No CEP equivalent at GMO, but the EPS drivers are similar**

Although GMO does not have an equivalent to the CEP, it is a part-owner in many of KCP&L's projects, including Iatan Units 1 and 2. This, in our opinion, diminishes the regulatory risk for GMO because we believe the Missouri regulators are unlikely to disallow the same investments that they have already determined are prudent for another utility, in this case KCP&L. This should shield GMO and, by extension, GXP from the potential for undue regulatory burden.

**The environmental retrofit of LaCygne 1 was initially part of the CEP, but was subsequently delayed as high demand for pollution control equipment resulted in shortages and concurrent price spikes.**

**Environmental retrofits should remain a key capital spending driver near term**

The scale, scope and effective regulatory pre-approval of capital investment under GXP's CEP are unlikely to be matched in the near term, in our view. However, we anticipate the installation of environmental control equipment that GXP is required to make on some of its coal plants to translate into sizeable capital investment opportunities over the next five years, and to continue to drive rate base growth. For example, GXP is required to meet more stringent emissions requirements under Best Available Retrofit Technology (BART) standards at its coal units by 6/1/2015. Great Plains has already announced plans to retrofit the two LaCygne units, and is evaluating similar options for Sibley 3, Lake Rose 6, Montrose 3, and Westar Energy's Jeffrey Energy Center (in which GMO is a partial 8% owner). These investments could add over \$1 billion to the rate base. Without the relative regulatory certainty under the CEP, however, the attractiveness of these investment opportunities will be determined by the regulatory treatment that they receive, which we do not expect to have good visibility into for some time.

**Transmission investments typically take 5-10 years from start to finish, owing to the difficulty in siting and permitting the lines.**

**Transmission investments should also contribute to rate base growth, though longer-dated in our view**

The transmission network of GXP's utilities is part of the regional grid of the Southwest Power Pool (SPP), the regional transmission organization in the area in charge of maintaining system reliability. SPP has approved several transmission projects as part of its regional infrastructure plan, some of which are in GXP's service territory. For example, Great Plains plans to build a 170-mile 345-kV line in GMO's service territory with an estimated cost of \$380 million, which the company plans to invest in the 2012-2017 timeframe. We also believe that additional projects are likely to be approved for construction over the next several years on the heels of years of palpable under-investment in the electrical grid. Hence, transmission investments could also be a meaningful driver for rate base growth going forward, although we caution that they are likely to have longer lead times relative to other types of infrastructure spending given the significant siting and permitting hurdles associated with transmission projects in general.

**RPS in KS and MO bode well for investments in renewable generation, too**

The recent passage of a renewable portfolio standard (RPS) in Kansas could present an opportunity for Great Plains to invest in additional renewable generation in the

medium and longer term. Kansas has a renewable portfolio standard (RPS) that requires 20% of each utility's peak capacity to be sourced from renewables by 2020, with intermediate targets of 10% by 2011, and 15% by 2016. Missouri adopted an RPS in 2008, mandating a 15% renewable energy requirement by 2021. Both of these regulatory requirements could present an opportunity for Great Plains to invest in additional renewable generation in the medium and longer term. We caution, however, that growth in renewable generation may not be as robust as each state's RPS suggests if the company chooses to satisfy its obligation through purchase power agreements rather than by building renewable generation in-house. We also note that the corresponding impact on customer bills in both states is limited to 1% per year, which may act as a deterrent to significant capital investment in renewables by the utilities.

#### **Clarity on nuclear strategy unlikely in the near term**

The Governor of MO has engaged in conversations with the utilities in the state and with interveners about repealing the current law that bans utilities from recovering nuclear construction costs prior to project completion. In recent conversations, GXP management reiterated that the company is supportive of the proposed legislative change, and views this as the necessary first step to engaging in further discussions about potentially investing in new nuclear generation. Great Plains announced recently its interest in exploring the possibility of building an additional unit at the Callaway nuclear site along with plant owner Ameren Corp. However, we believe that an investment decision around new nuclear generation is some ways down the road, if ever, and we therefore do not view it as a realistic growth driver in the medium term.

### **One Rate Case Down in KS...**

#### **Rate case decision and background**

GXP filed a rate case in Kansas in December 2009 for the Kansas jurisdictional portion of KCP&L (Docket No. 10-KCPE-415-RTS). The filing sought to recover mainly the utility's investment in Iatan Unit 2, as well as remaining investments in Iatan common plant and environmental upgrades on Iatan Unit 1 that were not captured in prior regulatory filings. In November 2010, the Kansas Corporation Commission (KCC) approved a \$21.8 million (4.6%) rate increase for KCP&L-Kansas premised upon a 10% ROE, 49.7% equity and a rate base of \$1.781 billion. This compares to the company's request for a \$55.1 million (11.5%) rate hike based on an 11.25% ROE and 46% equity, which was subsequently revised to a \$50.9 million ask and a 10.75% ROE following a partial settlement with intervenors. We estimate that the ROE differential vs. the original filing equates to about \$17 million on a revenue-equivalent basis. New rates became effective on 12/1/2010.

#### **Constructive rate case resolution in KS, though KS is the more supportive jurisdiction, in our opinion**

Although the authorized rate increase is below the company's request, it is also well above the KCC Staff's recommended metrics, namely a \$9.1 million increase and a 9.7% ROE. We consider this as a fairly constructive regulatory outcome, but note that Kansas in our opinion is a less contentious regulatory jurisdiction than Missouri, meaning that regulatory risk remains heightened for the balance of the company.

**Constructive outcome in KS is important, but KS represents only 28% of total sales, so an uphill battle is still ahead**

**Relatively small disallowance for a large capital investment is a net positive**

All capital expenditures under the CEP are subject to a prudence review, albeit with pre-determined hard caps on potential disallowances. The KCC adopted KCP&L's own proposal for Iatan 2 project disallowances of \$20.4 million, of which \$5.1 million reflects the KS jurisdictional portion. The KCC furthermore required minimal disallowances of \$1 million for the environmental retrofit of Iatan 1 and Iatan common plant (\$3.2 million on a total project basis). Relative to the size of the multi-million-dollar construction spending program, we believe these disallowances are fairly small, which supports our view of constructive regulation in the state of KS and, more importantly, sets a precedent for the pending MO rate cases.

**Denial of environmental tracker may preclude timely recovery of future environmental spending**

The KCC denied KCP&L's request for an environmental cost recovery rider (ECRR) similar to the one utilized by Westar Energy, GXP's neighboring utility in Kansas. Unlike Westar's rider, KCP&L's request incorporating the recovery of incremental O&M costs associated with environmental projects. Spending trackers are one of the key mechanisms to mitigate regulatory lag in jurisdictions that employ a historical rate making process. Hence, we believe the KCC decision may limit GXP's ability to recover future environmental capex on a timely basis, perpetuating the existing regulatory lag. KCP&L had proposed to use the ECRR to recover capital expenditures associated with the necessary environmental retrofits at the two LaCygne coal-fired units, which are required to be implemented by 6/1/2015. The KCC cited several reasons for its decision, including that the LaCygne retrofits constitute a significant capital investment which the ECRR is ill-suited to deal with, that the proposed ECRR schedule was identical to Westar's which would place an undue burden on the Commission calendar, and that GXP had agreed to forego a similar rider in MO until 2015. We note, however, that KCP&L may negotiate a different recovery mechanism, or use the existing predetermination statute, which enables companies to obtain regulatory pre-approval certifying prior to construction that a project is needed and its estimated costs are reasonable.

**The instant ECRR rejection does not preclude GXP from applying for a modified tracker or from using the predetermination statute**

**Other issues resolved in the rate case should not have a material near-term impact**

The current rate case resolved several issues as well; however, we don't expect any one of them to have a material impact on the stock in the near term. KCPL's proposals to modify and continue to use its current pension benefit tracker, which expires upon the completion of the CEP, was denied by the KCC. The Commission also denied the company's request to file an abbreviated rate case to true up any final adjustments to the Iatan construction costs, viewing it as premature. We do not consider either of these issues as critical for the company going forward, and do not expect them to have a material adverse impact in the near term.

**... But Several More to Go Through in MO**

With three rate cases currently pending in MO, we anticipate the first half of 2011 to be a busy time for Great Plains Energy as the Missouri utilities seek to recover in rates the final capital expenditures related to Iatan 2. Although we expect rate case activity to ultimately boost the company's earnings power in 2011 and 2012, we also anticipate disproportionate headline risk, which tempers our enthusiasm in the next several months.

**Lack of near-term earnings visibility is one of our main concerns for GXP investors.**

**3 rate cases pending in MO hinder near-term EPS visibility**

Great Plains filed a series of rate cases with the Missouri Public Service Commission (MPSC) in June 2010 in order to recover the MO portion of its investment in Iatan Unit 2, as well as the cost of common Iatan facilities and Iatan 1 costs not previously recovered. The Missouri filings came half a year later than KCP&L's KS rate case due to the delay in the start-up of Iatan 2, which was originally expected earlier in 2010. Pursuant to Missouri's regulatory policies, the power plant had to be online before the MPSC could consider the corresponding capital investment and to include it in rate base. Table 1 below summarizes the requested rate increases and return and asset base parameters sought by the company.

Table 1: Rate Cases Filed in Missouri

Utility	Case No.	Rate Increase	ROE	Rate Base (\$ mil)	Rates Effective
KCP&L - MO	C-ER-2010-0355	\$92.1	11.0%	\$2,123	5/4/2011
GMO - MPS	C-ER-2010-0356 (MPS)	\$75.8	11.0%	\$1,469	6/4/2011
GMO - L&P	C-ER-2010-0356 (L&P)	\$22.1	11.0%	\$422	6/4/2011

Source: Company reports and J.P. Morgan estimates.

**Initial MPSC Staff recommendations are a poor guideline for the final outcome, in our view, given that they do not incorporate all assets.**

**Staff recommendations are not final, but 9% ROE underscores unfavorable regulation**

The MPSC Staff filed testimony under each of the three pending dockets in November 2010, which are summarized in Table 2 below. Although the recommended rate increases appear significantly below the company's requests at a first glance, we note that Staff's recommendations do not take into account plant additions completed after 6/30/2010, which will be trued up in subsequent Staff testimony expected to be filed with the Commission in early 2011. Staff furthermore indicated that the latter may substantially change its recommendations. Thus, we believe that it is premature to use Staff's preliminary rate increase figures as a reference point, but caution that the 9% recommended ROE is unlikely to be revised upward. In our opinion, a 9% ROE is significantly below equity returns in other jurisdictions, and would be a further negative sign for Missouri regulation if adopted by the MPSC. Consequently, we remain cautious observers of the further progression of the regulatory calendar in the state for now.

Table 2: MPSC Staff Recommendations

Utility	Case No.	Rate Increase	% of Ask	ROE	Rate Base (\$ mil)
KCP&L - MO	C-ER-2010-0355	\$7.0	7.6%	9.0%	\$1,843
GMO - MPS	C-ER-2010-0356 (MPS)	\$5.5	7.3%	9.0%	\$1,180
GMO - L&P	C-ER-2010-0356 (L&P)	\$30.7	138.9%	9.0%	\$486

Source: Company reports and J.P. Morgan estimates.

**MO evidentiary hearings:**

**KCP&L: 1/18-2/4/2011**  
**GMO: 2/14-2/18/2011**

**We remain on the sidelines at least until the hearings are completed in light of MO's contentious regulatory framework**

Missouri regulation has traditionally been marked by contentious proceedings and below-average authorized returns. Consequently, we anticipate the hearings scheduled in the individual proceedings to be fairly contentious and therefore a potential source of headline risk. Therefore, we recommend that investors remain on the sidelines at least until the hearings phase in the rate cases is completed and regulatory risk dissipates. When regulatory visibility improves, we would be ready to revisit our investment thesis.



## Other Regulatory Concerns Expected to Persist

We expect key regulatory concerns such as regulatory lag and the lack of full fuel pass-through in some of Great Plains Energy's jurisdictions to persist, and to remain risk factors for equity investors. Fuel risk is partly mitigated near-term in our view by the current depressed commodity cost environment.

### **Regulatory lag remains an issue, particularly with large environmental retrofits looming on the horizon**

Neither Kansas nor Missouri employs prospective rate making, which, in our opinion, could be a meaningful risk factor during periods of significant capital spending. We do not anticipate major changes to regulation in either state in the short run. Although Great Plains has had some success with innovative strategies such as the Comprehensive Energy Plan, we are skeptical of the company's ability to negotiate a similar plan going forward in the still relatively depressed economic environment. GXP may be able to reduce regulatory lag by employing tracking mechanisms for specific types of capex, although we think the recent rejection of an environmental tracker in Kansas is not an encouraging start. We note that GXP has applied for transmission spending trackers in Missouri, which would be a positive if approved. Continuing to work with its regulators in both states to find ways that mitigate regulatory lag should remain a critical priority for GXP, in our view.

### **Current ban on use of CWIP in Missouri is a challenge, but may be repealed**

Missouri legislation prohibits the use of construction work in progress (CWIP) since a 1976 popular vote banned its use. This limits a utility's ability to recover construction costs until after a plant or other equipment has been placed in service, which presents a challenge in recovering capital spending associated with large investment projects. Recently, the Missouri Governor expressed a renewed interest in repealing the law; however, we believe that these discussions are in the preliminary stages and it is therefore unclear whether they will result in an actual change. We also note that several interest groups sought to repeal the CWIP provision in the 2009 legislative session, but ultimately failed. Given the history in the state, we anticipate the renewed repeal effort to be contentious and passage questionable.

### **Lack of complete fuel pass-through introduces commodity risk exposure**

KCP&L has a conventional fuel clause in Kansas, allowing it to pass a 100% of fuel and purchased power costs to customers. The utility does not have a similar mechanism in Missouri, however, where KCP&L-MO agreed not to seek a fuel clause until 2015 as part of the negotiating the CEP. KCP&L's Missouri jurisdictional portion of wholesale sales (about 55%) is credited back to retail customers, although the real risk for the company stems from the fact that wholesale margins are estimated prospectively and incorporated in rates, exposing the utility to under- or over-earning relative to this amount if actual wholesale sales differ from the forecast. Although the shortfall or over-earning is adjusted in the next rate case, this mechanism exposes the company to short-term earnings fluctuations. Finally, GMO's exposure to commodity prices has been limited since 2008 when the utility was allowed to pass 95% of electric fuel and purchased power costs to consumers through a fuel adjustment clause (FAC), and 80% of steam costs through a quarterly cost adjustment (QCA) mechanism. The steam business comprises an insignificant portion of the whole company (less than 1%), and, therefore, we do not see the 20% that may potentially not be recovered as a significant risk factor for the company. In the pending rate case, however, Staff recommended a sharing mechanism that would

only allow GMO to pass 75% of its fuel costs to consumers, potentially leaving shareholders on the hook for the rest. If approved, this would be a material deterioration in GMO's position.

## Earnings and Cash Flow Analysis

### Revising 2010-2012 earnings estimates

We are increasing our 2010 earnings estimate to \$1.60 from \$1.45 previously to incorporate YTD results, including the benefit of above-normal weather in GXP's service territory. We are modestly lowering our 2011E EPS to \$1.60 from \$1.70 previously to account for the delay in the in-service date of Iatan 2, which in turn pushes out some of the benefit of anticipated rate relief. Finally, we are adjusting our 2012E estimate to \$1.65 from \$1.75 per share after fine-tuning our cost and dilution assumptions. Our estimates assume that Great Plains's Missouri utilities receive about half of their respective requested rate relief in the pending rate cases. We also anticipate the MPSC to maintain the current regulatory calendar, with new rates in service 5/4/11 for KCP&L-Missouri and 6/4/11 for GMO. Any further delays could have a negative impact on our earnings forecast.

### Expect FCF to remain negative while capex levels remain elevated

Our model assumes that Great Plains remains free cash flow negative at least through 2013-2014 while environmental and other capital spending needs remain at elevated levels. Assuming relatively timely recovery of capital spending in rates and healthy earned returns on capital, we do not view the negative FCF in and of itself as a reason for concern. We do, however, believe that a supportive regulatory environment would play a pivotal role in investors' level of comfort with the company's ambitious capex plans.

### Dilution from the equity linked units in mid-2012 to pressure 2012-2013 EPS

Our 2012E EPS assume incremental dilution from the company's existing equity units. Great Plains issued 5.75 million equity units in mid-2009 with proceeds of \$287.5 million, which are mandatorily convertible no later than 6/15/2012. Our forecast assumes that each unit converts into 2.9762 common shares, equivalent to 17 million additional shares, which is consistent with a share price above \$16.80 per share. This is the main factor that partially offsets the positive impact of having new rates in effect for a full year in 2012. We note, however, that converting the equity units into straight equity also improves GXP's equity ratio, making another equity issuance highly unlikely through 2013. Finally, we expect the company to remarket the 10% subordinated notes underlying the equity units in the 6 months preceding the mandatory conversion date and to replace them with less expensive form of financing, which should lower interest costs in 2012 and beyond.

### Expect leverage to improve with the conversion of the equity units

We project overall leverage to decline to ~ 53% by the end of 2012 from ~ 57% expected in 2010 after the equity units convert into straight equity in mid-2012. The improving balance sheet position is consistent with the company's stated desire to focus on improving its credit metrics over time, which are somewhat weakened on the heels of the 5-year CEP. Our forecast assumes that GXP would not need to issue additional equity over this timeframe

**Since the equity units were excluded from the regulatory capital structure in KS, GXP would have to file another rate case in 2012 in order to have the additional equity reflected in rates.**

## Valuation and Rating Analysis

We are assuming lead analyst coverage of Great Plains Energy and are maintaining our Neutral rating. Although GXP shares could offer investors attractive EPS growth in 2012, we believe it is too early to get aggressive with the stock given that significant amount of regulatory risk remains while the Missouri utilities are going through their rate cases. Longer-term, we remain concerned about the detrimental impact of regulatory lag on earnings in both Missouri and Kansas, particularly since Great Plains is faced with meaningful environmental capital spending requirements through 2015. Accordingly, we recommend that investors remain on the sidelines at least until the hearings in the Missouri rate cases are completed and earnings visibility improves.

### Earnings growth already reflected in valuation, in our view

GXP shares currently trade at a 2011 P/E multiple of 12.1x, or at a discount of about 10% vs. the purely regulated peer group multiple. Although the appropriate discount should be somewhat lower in our view, or about 5%, the implied upside is not sufficient to get us to be more constructive on the stock yet. Furthermore, even though the shares screen relatively cheap on 2012E EPS, we believe the regulatory risk to GXP's 2012 earnings power remains above-average and therefore warrants discounted valuation. Hence, we expect the pending rate cases in Missouri to continue to weigh on GXP shares in the near term as regulatory uncertainty dominates the stock. As a result, we are maintaining our Neutral rating on the stock, and would revisit our investment thesis on the stock as we get more visibility into the company's 2012 earnings power.

Table 3: Relative P/E Valuation

Valuation at Group P/E Multiple	2010E	2011E	2012E
JPM GXP EPS Estimate (\$/share)	15.1x	13.9x	12.9x
Group Average P/E	-5.0%	-5.0%	-5.0%
Assumed Premium/Discount (%)	14.4x	13.2x	12.3x
Implied P/E for Valuation	<b>\$22.98</b>	<b>\$21.11</b>	<b>\$20.28</b>
GXP Valuation at Group Multiple	18.9%	9.2%	4.9%
Upside/Downside (%)	4.3%	4.5%	4.7%
Dividend Yield (%)	23.2%	13.7%	9.7%
<b>Total Return Potential (%)</b>	15.1x	13.9x	12.9x

Source: Company reports and JPMorgan estimates.

### Adjusting our December 2011 PT to \$21

We are lowering our December 2011 price target to \$21 per share from \$24 previously to reflect our updated earnings forecast, current group multiple and a modest discount to the group multiple to reflect the residual regulatory overhang associated with the pending rate cases. We believe that GXP shares should trade at a modest discount of about 5% vs. the 2011 average pure-play regulated utility P/E multiple 13.9x, which we apply to our updated 2011E EPS of \$1.60 to derive our price target. In our view, the regulatory risk associated with GXP's pending rate cases in MO warrants a modest discount to account for the potential headline risk and uncertainty, but the discount may dissipate if the regulatory outcomes turn out to be favorable. Finally, our discounted valuation also incorporates the regulatory lag that GXP experiences under its current rate-making mechanisms.

## Great Plains Energy: Summary of Financials

Income Statement - Annual	FY09A	FY10E	FY11E	FY12E	Income Statement - Quarterly	1Q10A	2Q10A	3Q10A	4Q10E
Sales	1,965	2,313	2,466	2,539	Sales	-	-	-	-
COGS	589	701	751	770	COGS	-	-	-	-
D&A	302	339	373	394	D&A	-	-	-	-
Operations and maintenance	754	795	834	851	Operations and maintenance	-	-	-	-
Other expenses	-	-	-	-	Other expenses	-	-	-	-
Total operating expenses	1,645	1,835	1,958	2,014	Total operating expenses	-	-	-	-
Other income / (expense)	43	35	15	10	Other income / (expense)	-	-	-	-
<b>EBIT</b>	<b>363</b>	<b>513</b>	<b>522</b>	<b>535</b>	<b>EBIT</b>	-	-	-	-
<b>EBITDA</b>	<b>665</b>	<b>852</b>	<b>895</b>	<b>928</b>	<b>EBITDA</b>	-	-	-	-
Interest expense	181	185	188	176	Interest expense	-	-	-	-
Income tax provision	30	112	114	122	Income tax provision	-	-	-	-
Tax rate	16.2%	34.0%	34.0%	34.0%	Tax rate	-	-	-	-
Discontinued operations and other	(2)	0	0	0	Discontinued operations and other	-	-	-	-
Preferred dividends	2	2	2	2	Preferred dividends	-	-	-	-
<b>Net income</b>	<b>148</b>	<b>214</b>	<b>219</b>	<b>235</b>	<b>Net income</b>	-	-	-	-
Total non-recurring items	2	0	0	0	Total non-recurring items	-	-	-	-
<b>Net income (Recurring)</b>	<b>150</b>	<b>214</b>	<b>219</b>	<b>235</b>	<b>Net income (Recurring)</b>	-	-	-	-
Diluted shares outstanding	130	136	136	144	Diluted shares outstanding	-	-	-	-
Diluted EPS	1.15	1.60	1.60	1.65	Diluted EPS	-	-	-	-
DPS (\$)	0.83	0.83	0.87	0.92	DPS (\$)	-	-	-	-
Payout ratio	71.5%	52.4%	54.0%	56.1%	Payout ratio	-	-	-	-
Balance Sheet and Cash Flow Data	FY09A	FY10E	FY11E	FY12E	Ratio Analysis	FY09A	FY10E	FY11E	FY12E
Cash and cash equivalents	66	0	0	0	Sales growth	17.7%	17.7%	6.6%	3.0%
Current assets	547	547	547	547	EBITDA growth	25.2%	28.2%	5.0%	3.7%
PP&E	6,651	6,988	7,300	7,574	EBIT growth	22.5%	41.4%	1.8%	2.4%
Non-current assets	1,219	1,224	1,229	1,234	Net income (recurring) growth	27.2%	42.8%	2.0%	7.4%
<b>Total assets</b>	<b>8,483</b>	<b>8,759</b>	<b>9,076</b>	<b>9,355</b>	COGS growth	13.2%	18.9%	7.2%	2.5%
Current liabilities	958	1,366	1,882	981	Total operating expenses growth	17.9%	11.6%	6.7%	2.9%
Long-term Debt	3,213	2,980	2,680	3,468	Diluted EPS growth	(1.3%)	39.1%	0.0%	3.1%
Preferred stock	39	39	39	39	Gross margin	70.0%	69.7%	69.5%	69.7%
Other non-current liabilities	1,479	1,479	1,479	1,479	Operating margin	22.5%	41.4%	1.8%	2.4%
Common equity	2,794	2,896	2,996	3,387	Debt / Capital (book)	56.3%	56.6%	57.1%	53.4%
Total liabilities & equity	8,483	8,759	9,076	9,355	Times interest earned	2.0	2.8	2.8	3.0
Net income	148	214	219	235	FFO / Interest	3.5	4.1	4.2	4.7
D&A	302	339	373	394	FFO / Debt	17.4%	19.7%	19.6%	20.8%
Change in working capital	(118)	0	0	0	ROE	5.4%	7.4%	7.3%	6.9%
Change in other assets	0	0	0	0	Return on invested capital (ROIC)	3.1%	4.3%	4.3%	4.3%
<b>Net operating cash flow</b>	<b>335</b>	<b>569</b>	<b>606</b>	<b>643</b>					
<b>Cash flow from investing activities</b>	<b>(898)</b>	<b>(697)</b>	<b>(704)</b>	<b>(688)</b>					
Net common equity issued/(repurchased)	220	0	0	288					
Net debt issued/(repurchased)	484	175	216	(112)					
Common dividends paid	(110)	(112)	(118)	(132)					
Other financing activity	(27)	0	0	0					
<b>Cash flow from financing activities</b>	<b>567</b>	<b>62</b>	<b>98</b>	<b>44</b>					
Increase/(decrease) in cash	5	(66)	0	0					
Cash at beginning of the period	61	66	0	0					
Cash at end of the period	66	0	0	0					

Source: Company reports and J.P. Morgan estimates.

Note: \$ in millions (except per-share data). Fiscal year ends Dec

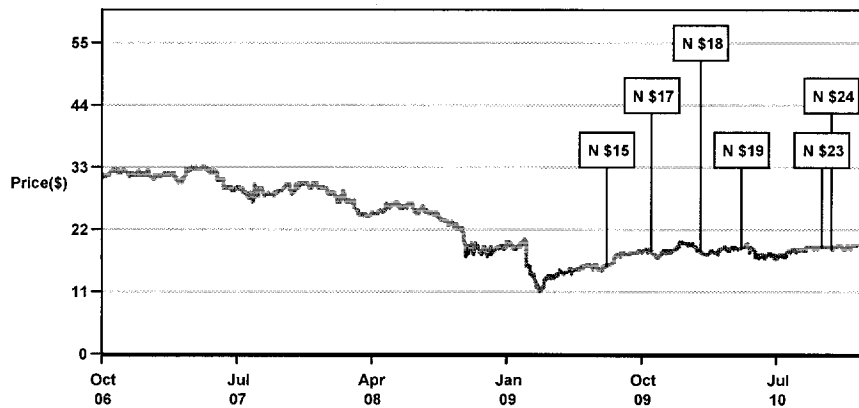
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Great Plains Energy (GXP) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
22-Jul-09	N	15.44	15.00
22-Oct-09	N	18.30	17.00
26-Jan-10	N	18.31	18.00
20-Apr-10	N	18.76	19.00
29-Sep-10	N	18.80	23.00
22-Oct-10	N	18.74	24.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Jul 22, 2009. This chart shows J.P. Morgan’s continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. J.P. Morgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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