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AUTH.NAME AUTHOR AFFILIATION
VAN BRUNT,E.E. Arizona Public Service Co.
RECIP.NAME RECIPIENT AFFILIATION
Office of Nuclear Reactor Regulation

SEE REPORT #50-528

SUBJECT: Forwards AZ Public Svc Co,PSC of NM,El Paso Electric Co & Southern CA Edison Co Annual Financial Repts 1979. See Report

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ARIZONA PUBLIC SERVICE COMPANY

P. O. BOX 21666 · PHOENIX, ARIZONA 85036

May 13, 1980
ANPP-15429 - JMA/JPS

Director of Nuclear Reactor Regulation
U.S. Nuclear Regulatory Commission
Washington, D.C. 20555

Re: Palo Verde Nuclear Generating Station
Units 1, 2 and 3
NRC Docket Nos. STN 50-528/529/530

Dear Sir:

Pursuant to 10 CFR Part 50.71(b), Arizona Public Service Company (APS) submits herewith two (2) copies of the 1979 financial statements for each of the Participants who jointly own the Palo Verde Nuclear Generating Station.

Respectfully submitted,

ARIZONA PUBLIC SERVICE COMPANY

By: Edwin E. Van Brunt
Edwin E. Van Brunt, Jr.
Vice President

On its own behalf and as agent for all other joint participants

EEVBJr/JPS/av
Attachment
cc: J. Kerrigan

STATE OF ARIZONA)
) ss.
County of Maricopa)

Subscribed and sworn to before me this 15 day of MAY, 1980.

John M. Allen
Notary Public

My Commission expires:
My Commission Expires Jan. 23, 1983

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ARTHUR ANDERSEN & CO.
PHOENIX, ARIZONA

To the Board of Directors,
Salt River Project Agricultural Improvement and Power District, and

Board of Governors,
Salt River Valley Water Users' Association:

We have examined the combined balance sheets of SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT (a political subdivision of the State of Arizona) and its agent, SALT RIVER VALLEY WATER USERS' ASSOCIATION, together referred to as the SALT RIVER PROJECT, as of December 31, 1979 and 1978, and the related combined statements of net revenues and sources of funds for additions to utility plant for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the Salt River Project as of December 31, 1979 and 1978, and the results of its operations and sources of funds for additions to utility plant for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Arthur Andersen & Co.

Phoenix, Arizona,
February 15, 1980.

SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT

AND ITS AGENT, SALT RIVER VALLEY WATER USERS' ASSOCIATION

COMBINED BALANCE SHEETS - DECEMBER 31, 1979 AND 1978

ASSETS

($000)	1979	1978
UTILITY PLANT, at original cost (Notes 1, 2, 3 and 4):		
Plant in service-		
Electric	$1,467,048	$ 891,865
Irrigation	67,381	66,140
General	51,792	44,468
Total plant in service	1,586,221	1,002,473
Less- Accumulated depreciation on plant in service	286,099	254,019
	1,300,122	748,454
Construction work in progress	769,562	909,666
	2,069,684	1,658,120
SEGREGATED FUNDS, consisting of cash, U. S. Government obligations and bankers' acceptances set aside in accordance with resolutions of bond issues:		
Debt service funds, excluding $54,768,000 in 1979 and $47,156,000 in 1978 for payment of accrued interest (Note 5)	138,540	118,487
Construction funds	246	491
	138,786	118,978
CURRENT ASSETS:		
Cash	396	524
Temporary investments, at cost, held primarily for construction	115,631	119,938
Deposit in debt service fund for payment of accrued interest on bonds	54,768	47,156
Trade and other accounts receivable, less reserves of $1,455,000 in 1979 and $1,335,000 in 1978 for doubtful accounts	37,335	38,621
Fuel stocks, at average cost	77,427	15,221
Materials and supplies, at average cost	20,625	14,926
Prepayments, interest receivable and other	9,935	8,387
	316,117	244,773
DEFERRED CHARGES AND OTHER ASSETS (Note 1)	59,249	47,053
	$2,583,836	$2,068,924

CAPITALIZATION AND LIABILITIES

($000)	1979	1978
LONG-TERM DEBT (Note 5):		
Electric system revenue bonds	$1,658,844	$1,386,725
General obligation bonds and other	255,236	269,289
	1,914,080	1,656,014
ACCUMULATED NET REVENUES, invested principally in utility plant:		
Balance beginning of year	276,684	210,891
Net revenues for the year	100,435	65,793
Balance end of year	377,119	276,684
Total capitalization	2,291,199	1,932,698
CURRENT LIABILITIES, excluding $18,999,000 in 1979 and $16,132,000 in 1978 representing current portion of long-term debt which is to be paid from segregated funds:		
Notes payable to banks (Note 7)	120,000	-
Accounts payable	74,302	50,635
Accrued taxes and tax equivalents (Note 6)	18,419	17,875
Accrued interest	56,044	47,156
Customers' deposits	6,440	5,255
Other current and accrued liabilities	7,271	6,572
	282,476	127,493
DEFERRED CREDITS AND RESERVES	10,161	8,733
COMMITMENTS AND CONTINGENCIES (Notes 3 and 6)		
	$2,583,836	$2,068,924

The accompanying notes are an integral part of these combined balance sheets.

SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT

AND ITS AGENT, SALT RIVER VALLEY WATER USERS' ASSOCIATION

COMBINED STATEMENTS OF NET REVENUES

FOR THE YEARS ENDED DECEMBER 31, 1979 AND 1978

	($000) 1979	($000) 1978
OPERATING REVENUES:		
Electric	$413,066	$333,329
Water and irrigation	4,723	4,435
Total operating revenues	417,789	337,764
OPERATING EXPENSES:		
Power purchased	25,020	23,449
Fuel used in electric generation	100,352	73,050
Other operation expenses	57,876	52,051
Maintenance	32,508	29,201
Depreciation and amortization (Note 1)	32,995	30,806
Taxes and tax equivalents (Note 6)	42,859	38,340
Total operating expenses	291,610	246,897
Net operating revenues	126,179	90,867
FINANCING COSTS:		
Interest on bonds at coupon rates	104,964	88,125
Amortization of bond discount	1,100	953
Amortization of bond issue expense	231	211
Amortization of loss on defeased debt	976	901
Interest on other obligations	6,475	1,797
Interest earned on investments and deposits	(28,841)	(25,059)
Net financing costs	84,905	66,928
Less- Allowance for funds used during construction (Note 1)	(59,735)	(42,183)
Financing costs less allowance for funds used during construction	25,170	24,745
OTHER DEDUCTIONS, net	574	329
NET REVENUES FOR THE YEAR	$100,435	$ 65,793

The accompanying notes are an integral part of these combined statements.

SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT AND ITS AGENT, SALT RIVER VALLEY WATER USERS' ASSOCIATION

COMBINED STATEMENTS OF SOURCES OF FUNDS FOR ADDITIONS TO UTILITY PLANT

FOR THE YEARS ENDED DECEMBER 31, 1979 AND 1978

	($000) 1979	1978
GROSS ADDITIONS TO UTILITY PLANT, excluding allowance for funds used during construction	$394,728	$406,124
FUNDS GENERATED FROM OPERATIONS:		
Net revenues for the year	$100,435	$ 65,793
Add- Depreciation (including charges to clearing accounts) and other charges not requiring current funds	37,624	34,969
Deduct- Allowance for funds used during construction not providing current funds	(59,735)	(42,183)
Total funds generated from operations before retirement of debt	78,324	58,579
Less- Repayment of long-term debt	(16,167)	(15,393)
Net funds generated from operations	62,157	43,186
FUNDS OBTAINED FROM FINANCING:		
Proceeds of bond issues, less defeased bonds	273,122	239,588
Advances from U.S. Government for rehabilitation of irrigation plant	766	1,236
Contributions in aid of construction	7,582	7,898
Borrowings, net of repayments	119,256	926
Total funds obtained from financing	400,726	249,648
Other-		
Increase in segregated funds set aside for debt service	(20,053)	(13,417)
Decrease in segregated funds set aside for construction	245	49,856
Decrease in temporary investments held primarily for construction	4,307	26,517
Net funds obtained from financing	385,225	312,604
CHANGES IN OTHER ITEMS AFFECTING FUNDS:		
Decrease in receivable on sale of plant	-	47,480
Increase in unamortized loss on defeased debt	-	(6,639)
Increase in accounts payable	23,667	9,563
Decrease (increase) in accounts receivable	1,286	(7,413)
(Increase) decrease in fuel stocks and materials and supplies	(67,905)	5,998
Increase in deposits for payment of accrued interest on bonds	(7,612)	(8,300)
Increase in accrued interest	8,888	8,300
(Increase) decrease in cash	128	(183)
Change in other assets and liabilities, net	(11,106)	1,528
Net change in other items	(52,654)	50,334
FUNDS USED FOR ADDITIONS TO UTILITY PLANT	$394,728	$406,124

The accompanying notes are an integral part of these combined statements.

SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT

AND ITS AGENT, SALT RIVER VALLEY WATER USERS' ASSOCIATION

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 1979 AND 1978

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

(a) The Project's Board of Directors serves as its regulatory agent.

(b) Principles of Combination

The combined financial statements include the accounts of the Salt River Project Agricultural Improvement and Power District ("the District") and the accounts of its agent, the Salt River Valley Water Users' Association, together referred to as the Salt River Project ("the Project"), and a wholly owned subsidiary, Salt River Generating Company. All significant intercompany transactions have been eliminated.

(c) Utility Plant, Depreciation and Maintenance

The accounting records of the Project are maintained substantially in accordance with the Uniform System of Accounts prescribed for electric utilities by the Federal Energy Regulatory Commission. Utility plant is stated at the historical cost of construction. Construction costs include labor, materials, services purchased under contract, and allocations of indirect charges for engineering, supervision, transportation, and administrative expenses.

An allowance for funds used to finance construction work in progress is capitalized as a part of the electric and general plant. This allowance is deducted from net financing costs in the combined statements of net revenues and added to utility plant. Capitalization rates of 7.2% and 7.5% were used in 1979 and 1978, respectively.

Depreciation expense is computed on the straight-line basis over estimated useful lives of the various classes of plant. Rates in effect resulted in provisions approximating 3.49% for 1979 and 3.46% for 1978 on the average cost of depreciable electric plant, and 1.94% for 1979 and 1.93% for 1978 for depreciable irrigation plant. When property representing a retirement unit is replaced, removed, or abandoned, the cost of such property is credited to the appropriate utility plant account, and such cost together with removal costs less salvage is charged to accumulated depreciation.

The Project charges to maintenance expense the cost of labor, materials, and other expenses incurred in the repair, restoration of condition and replacement of minor items of property.

(d) Bond Expense

Bond discount, premium, and bond issue expense are being amortized over the terms of the related bond issues.

(e) Unamortized Loss on Defeased Debt

In April 1978 and August 1977 electric system revenue bonds were sold. Portions of the proceeds of these bonds were used to defease $210,000,000 of the outstanding electric system revenue bonds. These defeasances resulted in gross savings in debt service over the lives of the new issues of $32,300,000. The combined financing costs of the defeasances were $26,055,000. The District Board of Directors approved deferral of the financing costs and their amortization over the lives of the April 1978 and August 1977 issues.

(f) Employes' Retirement Plan

The Project has a retirement plan covering substantially all employes. The plan is funded entirely from employers' contributions and the earnings of the invested assets. The estimated unfunded past service liability, as determined by the plan's actuary using the "entry age normal cost" valuation method, with frozen initial liability, was $9,641,776 as of July 1, 1979. This amount is being funded and amortized over a period ending in 2009. The employers' contributions to this plan totaled $7,392,482 in 1979 and $5,970,882 in 1978.

At July 1, 1979, the plan's assets exceeded the actuarially computed value of the vested benefits at the same date.

(g) Revenues

Meters for residential, commercial and small industrial customers are read cyclically and sales recorded only when billed. This system of billing results in earned but unbilled revenues which amounted to $10,438,200 at December 31, 1979, and $8,956,000 at December 31, 1978. For large industrial customers, meters are read near month-end and billings recorded on the accrual basis. Electric revenue billings are adjusted periodically for changes in costs of fuel and purchased power. Revenues from water and irrigation operations are recorded when earned.

(h) Electric Rates

Under Arizona law, the District Board of Directors has the exclusive authority to establish electric rates. The District is required to follow certain procedures, including certain public notice requirements and holding a special Board meeting, before implementing any changes in the standard electric rate schedules. A general rate increase of 9.6% approved by the District's Board on January 29, 1980 becomes effective March 1, 1980.

(2) POSSESSION AND USE OF UTILITY PLANT:

The United States of America retains a paramount right or claim in the Project which arises from the original construction and operation of the Project's facilities as a Federal Reclamation Project. The Project's right to the possession and use of, and to all revenues produced by, these facilities is evidenced by contractual arrangements with the United States.

(3) CONSTRUCTION PROGRAM:

Balances shown for construction work in progress represent expenditures for new facilities required to serve anticipated customer needs, and consist of:

	December 31 ($000)	
	1979	1978
Electric generating facilities	$741,638	$828,371
Transmission and distribution	19,937	75,349
Irrigation plant	5,219	3,247
Other construction	2,768	2,699
Total	$769,562	$909,666

Construction expenditures planned for 1980 through 1984 approximate $328,200,000; $300,900,000; $197,500,000; $281,100,000 and $221,100,000, respectively.

At December 31, 1979, necessary commitments had been entered into for delivery of materials and services on construction projects. In addition, various firm commitments exist under coal and fuel oil supply contracts.

Palo Verde Nuclear Generating Station (PVNGS):

The Project has a 29.1% interest in PVNGS. From information now available the Project cannot assess whether the construction schedule used for Units 1, 2 and 3 will be affected by delays or moratoriums in the issuance of permits and licenses of the nature currently under review by Congress and the Nuclear Regulatory Commission as a result of the Three Mile Island incident.

Currently there is a contingency allowance to reflect the possibility of one year delays in the completion of Unit 2 and 3, and the possibility of more stringent regulatory requirements related to nuclear facilities. There can be no assurance that this provision will be adequate to cover possible increased costs associated with any major changes mandated by regulatory agencies as a result of the Three Mile Island incident.

Anti-nuclear groups active in Arizona are circulating petitions for ballot measures that purport to prohibit the construction and operation of any nuclear facilities in Arizona, including those now under construction, until certain conditions are met, and to deny recovery of expenses resulting from accidents and outages of such facilities to PVNGS participants whose rates are regulated by the Arizona Corporation Commission. If these measures are on the 1980 Arizona general election ballot, the PVNGS participants intend to actively oppose their approval.

(4) INTERESTS IN JOINTLY OWNED ELECTRIC UTILITY PLANTS:

The Project has entered into various agreements with other electric utilities for the joint ownership of electric generating and transmission facilities. Each participating owner in these facilities must provide for and furnish the financing for its ownership share. The following schedule reflects the Project's ownership interest (at cost) in jointly owned electric utility plant at December 31, 1979.

		In Millions		
Plant Name	Ownership Share Percent	Plant in Service	Accumulated Depreciation	Construction Work in Progress
Four Corners (New Mexico)	10.0	$ 21.0	$ 6.7	$ 3.1
Mohave (Nevada)	10.0	30.5	7.9	2.7
Navajo (Arizona)	21.7	200.6	29.5	.3
Hayden (Colorado)	80.0	102.1	11.7	.1
Coronado (Arizona)	70.0	439.8	.5	167.2
Craig (Colorado)	29.0	124.5	.1	78.0
Palo Verde (Arizona)	29.1	3.4	-	428.6
		$921.9	$56.4	$680.0

The Project's share of direct expenses of the jointly owned plants is included in the corresponding operating expenses in the combined statements of net revenues.

(5) LONG-TERM DEBT:

	Interest Rate	1979 ($000)	1978 ($000)	Future Maturities
Electric System Revenue Bonds (a):				
1973 Series A and B	5 to 6-1/2	$ 144,090	$ 145,885	1980-2011
1974 Series A and B	5.7 to 7.6	140,000	140,000	1983-2012
1976 Series A, B, C and D	4.0 to 7.2	405,000	405,000	1980-2016
1977 Series A, B Refunding and C	3-3/4 to 6-1/8	395,915	395,915	1980-2017
1978 Series A, B and C	4.4 to 7	317,900	317,900	1981-2018
1979 Series A, B and C	4-3/4 to 7-1/4	281,107	-	1983-2019
		1,684,012	1,404,700	
Unamortized bond discount		(25,168)	(17,975)	
Total electric system revenue bonds outstanding		1,658,844	1,386,725	
General Obligations Bonds and Other, 1% to 7.77% (b)		255,236	269,289	1980-2004
Total long-term debt		$1,914,080	$1,656,014	

(a) Electric system revenue bonds are secured by a pledge of, and a lien on, the revenues of the electric system after deducting "operating expenses", as defined in the bond resolutions, subject to prior liens of general obligation bonds of $241,074,998 and amounts due the United States of $12,545,337. In all years to date electric revenues, after deducting "operating expenses" as defined in the bond resolutions, have been more than sufficient to meet all debt service requirements.

(b) General obligation bonds are a lien upon the real property included in the District and are additionally secured by a pledge of revenues from the operation of the electric system. If the net electric revenues, as defined in the bond resolutions, are not sufficient to meet the principal and interest payments, the bonds and interest are payable from a levy of taxes on the real property.

The annual maturities of bonds and other long-term debt outstanding as of December 31, 1979 due in each of the years 1980 through 1984 are $19,524,000; $21,934,000; $22,814,000; $23,220,000 and $24,642,000, respectively.

Interest and amortization of discount on the various issues outstanding during the year resulted in an effective rate of 6.17% for 1979 and 6.04% in 1978. This rate approximates 6.40% over the remaining terms of the bonds.

The debt service portion of segregated funds includes $29,309,000 at December 31, 1979, and $22,463,000 at December 31, 1978, restricted for operating reserve requirements under bond resolutions.

Electric system revenue bonds totaling $405,888,000 principal amount are authorized, but unissued. Electric system refunding revenue bonds not to exceed $115,000,000 principal amount were also authorized, but unissued.

In March 1980, the District plans to issue Electric System Revenue Bonds (1980 Series A) for an estimated amount of $100,000,000.

(6) LITIGATION:

Environmental

Various pending litigation or administrative proceedings involving environmental matters could affect interests owned by the Project in present and proposed generating facilities. In general, these lawsuits seek to impose higher air quality standards for generating plants. If ultimately decided adversely to the interest of the Project, the outcome of the lawsuits could result in increased construction costs, increased future operating costs, and a possible loss in the operational reliability of certain generating plants. All of these effects would increase the costs to be passed on to customers through increased electric rates.

Property Valuation

Lawsuits filed by the State of Arizona against the Project to increase contributions in lieu of property taxes over the amounts already paid by the Project for the years 1970 through 1974 and 1978 were settled and $2,100,000 was paid in August, 1979 to the various taxing authorities in full and final settlement of all claims.

Navajo Tax

The Navajo Tribe has created a Tax Commission which claims authority to tax facilities on the Navajo Indian Reservation. The Tribe has adopted a possessory interest tax and a business activity tax on certain facilities and operations on the Reservation, and the District is informed that such taxes are intended to apply to the Navajo and Four Corners Projects. The District is unable to estimate the magnitude of the possessory interest tax because of its inability to interpret the way the tax is to be calculated. The District estimates that the business activity tax, if upheld by the courts, could expose it to claims approximating $4.6 million per year. The District and other Navajo and Four Corners Project co-owners have filed actions in the Federal District Court for Arizona and New Mexico contesting the validity and imposition of the taxes. The District has appealed a decision from Federal District Court for Arizona upholding the right of the Tribe to impose the possessory interest tax to the Ninth Circuit Court of Appeals.

The Navajo Tribal Council has adopted resolutions which, if valid, require permits and the quarterly payment of taxes for emission of sulphur at rates which commence at $.15 per lb. the first year and increase annually to $.75 per lb. in the fifth year. The District and other Navajo and Four Corners Project co-owners filed actions in Federal District Court for Arizona and New Mexico. The tax will become effective subsequent to either approval of the Secretary of the Interior or a finding by him that such approval is not required. If such tax is upheld by the courts, the District could be exposed to claims approximating $3 million in the first year and increasing to $15 million in the fifth year and each year thereafter.

The assertion by the tribal council of taxing and regulatory authority on the Navajo Indian Reservation has caused the Board of Directors of the District to adopt a resolution allowing it to recover from its customers the amounts of such taxes if the payment thereof is ultimately required.

Other

Principally as a result of certain water flooding in March and December 1978, various lawsuits have been filed against the Project alleging that the Project has a responsibility in regard to flood control and a liability in regard to flood damage. The ultimate liability, if any, is not determinable, but management expects that a significant portion of any liabilities which might result from flood damage claims will be covered by insurance.

(7) LINE OF CREDIT:

The District has a line-of-credit agreement with 14 banks, which provides for a maximum commitment of $120,000,000 with interest on borrowings at a rate equal to 60% of the banks' prime rate as established from time to time by a lead bank. No compensating balances nor commitment fees are required under the line of credit. The current agreement terminates on September 2, 1980. The line-of-credit borrowings are borrowed in the name of and payable from the General Fund and rank junior to payments required for the Prior Lien Bonds and the Revenue Bonds. At December 31, 1979, $120,000,000 was borrowed at an initial rate of 9.45%, payable on or before September 2, 1980.

(8) IRRIGATION AND WATER OPERATIONS:

The expenses, including depreciation, for irrigation and water operations exceeded the assessments, delivery fees, and other revenues therefrom by approximately $6,182,000 in 1979 and $7,507,000 in 1978. These amounts do not include expenditures for additions and improvements to irrigation plant and for repayment of long-term debt.

8005200594

LEDGER

To: December 31, 1979

From: January 1, 1979

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1979 Annual Report

PNM

Public Service Company of New Mexico

Index - 1979

The annual meeting of stockholders is scheduled to be held April 22, 1980. A proxy form and notice of the annual meeting will be mailed to all stockholders on March 3, 1980.

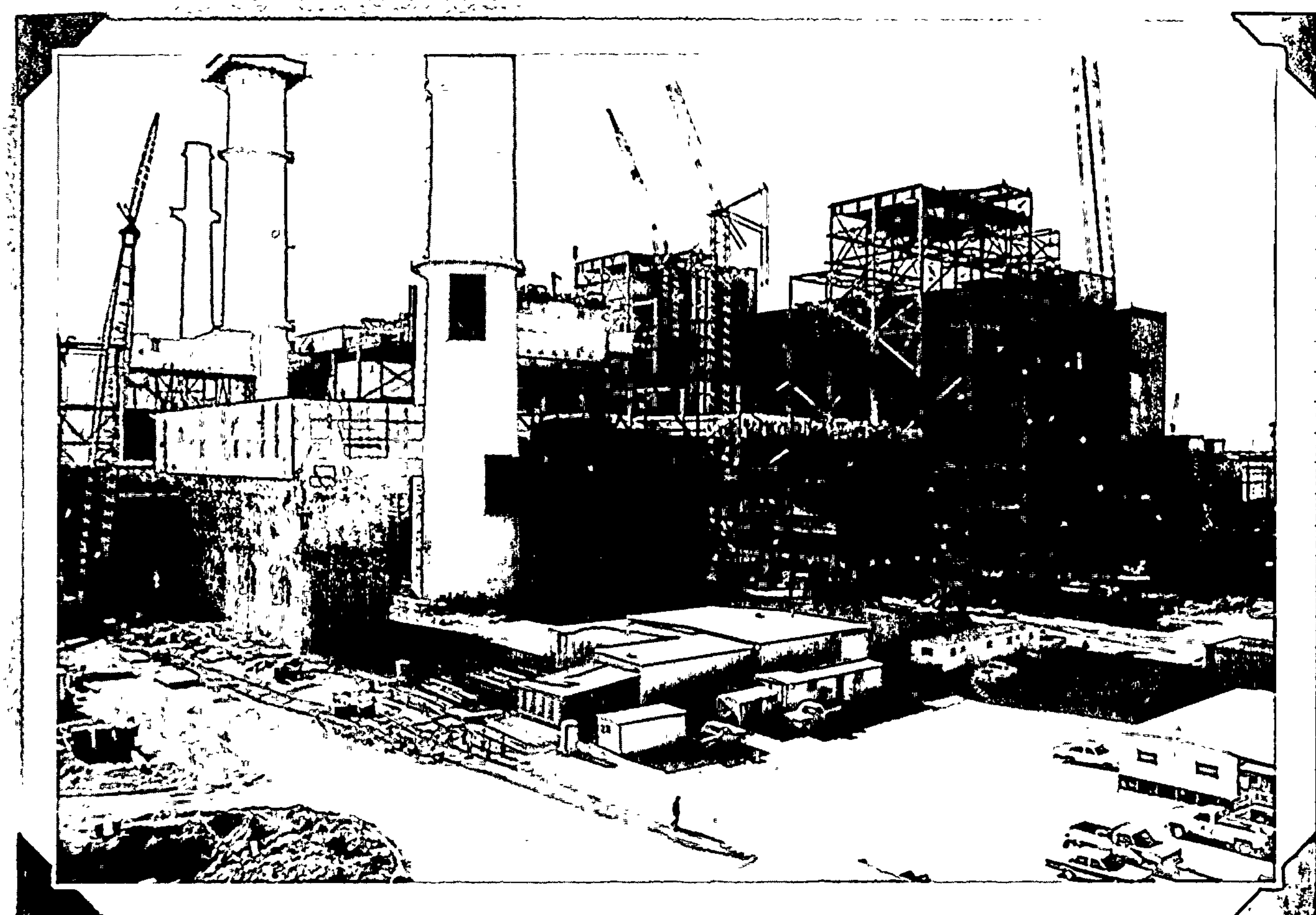
For further information and details pertaining to the information provided in this report contact D. E. Peckham, Secretary, Public Service Company of New Mexico, Post Office Box 2267, Albuquerque, New Mexico 87103.

The Common Stock of this Company is traded on the New York Stock Exchange under the symbol PNM.

This Annual Report and the financial statements contained herein are submitted for the general information of the stockholders of the Company and are not intended for use in connection with any sale or purchase of, or any offer or solicitation of offers to buy or sell, any securities of the Company.

Financial Highlights

	1979	1978	% Change
Operating revenues	$ 244,370,000	$187,205,000	30.5
Operating expenses	$ 184,554,000	$143,258,000	28.8
Operating income	$ 59,816,000	$ 43,947,000	36.1
Net earnings	$ 54,803,000	$ 37,464,000	46.3
Net earnings applicable to common stock	$ 42,607,000	$ 29,081,000	46.5
Return on average common equity	13.6%	13.0%	4.6
Average number of common shares outstanding	14,363,000	10,289,000	39.6
Net earnings per common share	$ 2.97	$ 2.83	5.0
Dividends paid per common share	$ 1.88	$ 1.72	9.3
Construction expenditures	$ 323,361,000	$198,976,000	62.5
Gross investment in utility property	$1,197,514,000	$879,893,000	36.1
Kilowatt-hour sales (thousand kWhr)	4,960,451	4,527,826	9.6
Number of electric customers served at year end	206,000	196,000	5.1
Average kWhr usage per residential customer	5,929	5,880	.8
Number of employees	2,311	2,054	12.5
Number of common stockholders	34,236	27,026	26.7



President's Letter

The end of a decade has come. For our industry, as for the country in general, it was ten years of unrelenting change. The rules and the perceptions of society, the attitude of the government and the attitude toward the government seemed to shift daily. It was a strange ten years no matter who you were or how you looked at it.

It was a decade which saw the United States disengage itself from a war which it neither bothered to declare nor set realistic military goals. It was a decade in which, for the first time, an American president resigned in disgrace. It was a decade that saw "liberals" begin to militantly support the status quo under the no-growth theme and "conservatives" argue heatedly for growth and change. It was a decade that saw the nation seemingly go into shock and refuse to make decisions or take action on matters of paramount importance — energy, defense, economic policy . . . the list is endless.

J.D. Geist, President

Yet, through it all, our institutions did manage to survive and to keep providing the public with far more than human history could define as "basic necessities." Life went on, although polls revealed that for the first time in American history many people no longer felt confident in the future.

As it became apparent that new ideas were going to be essential, it was decided that a touchstone was needed to help us all make sure we were looking in the right direction. A statement of principle was adopted. The full statement is on page 31. As simplistic as these thoughts may seem, it is only necessary to reflect for a moment on the complexities of life and the confusion surrounding us to see why a straightforward standard was developed. If PNM can adhere to these simple thoughts, our customers will have the service they expect at a price they can afford and in a manner they can understand. Our employees will have worthwhile jobs and our owners will be repaid for making it all possible.

An astounding expansion came about during this decade, in part, as people in other states began to develop an appreciation for the way of life offered by New Mexico. It also resulted from the commitment the people of New Mexico have made to their environment. The investment in pollution control equipment at the San Juan Generating Station now exceeds the total investment of the Company just ten years ago.

Meanwhile, as the nation and the world grappled with problems, companies, including PNM, had to come up with solutions to their own problems. In light of the range and diversity of the problems encountered in the 1970's, the last ten years may well go down as a decade of solutions for PNM.

PNM initiated a shift to coal without governmental suggestion or advice more than two decades ago. The third unit at the San Juan Generating Station came on-line in 1979. During the past year, your Company acquired full ownership of the fourth unit now under construction at San Juan. By this action, we can assure our customers that they will have electricity in the 1990's. Such assurance is becoming difficult for all utilities to make in these uncertain times.

However, using coal as an energy resource is not without its problems. Stringent constraints have been established on the burning of coal. PNM is committed to building and operating facilities to meet those requirements. When new regulations were being developed, and when regulatory actions were required, we often found that the desires of environmentalists compounded our already complex business environment. However, PNM has worked hard to establish a good relationship with local organized environmental groups. As a result, we have often been able to achieve agreements with those groups that contribute to the preservation of New Mexico's environment and maintain a balanced consideration of the customers' needs.

In addition, we continue to search for new and better ways to meet future needs without relying on natural gas and oil. As part of this search, work continued on the Palo Verde Nuclear Generating Station. As you know, your Company committed itself to a 10.2 percent share in that project in 1973. In the aftermath of Three Mile Island, extensive reviews of the engineering and construction at Palo Verde have been conducted and some are still underway. We are confident that Palo Verde will serve our customers safely and reliably. We are also confident that society will conclude that the benefits of having domestic energy resources beyond the control of international politics will outweigh the limited risks of nuclear energy.

PNM studies continue to demonstrate that nuclear power has economic, environmental, and safety advantages over other available generating alternatives. Even though this is the case, the nuclear option is currently plagued with political and regulatory uncertainties. Therefore, PNM has not made a commitment to the construction of a nuclear plant within New Mexico, but the Company does continue to include the nuclear option as a consideration in its generation planning activities. Such planning includes the examination of design options, economics, and feasible sites for any future projects.

Work will soon commence on PNM's and the country's first hot water geothermal generating facility. Though geothermal energy now provides a significant part of northern California's electricity, the hot dry steam used there is a geological rarity. Geothermal hot water is not as rare and, if the PNM project now under development with the Department of Energy and Union Oil Company is successful, the technology could lend itself to application in many areas of the country.

The decade of the 1970's was remarkable for both the nation and PNM. But changing the calendar has not changed all our problems; energy remains a critical issue; economics of uncertainty are still part of our everyday life; and the quest for understanding and solutions to these pressing issues will be the hallmark of the 1980's.

Your Company's requirements for new construction in the 1980-84 five-year period is predicted to be $1,084 million. This is less than in the 1979-83 period. Barring any unexpected circumstances, there will be little change in the real price of electricity in the foreseeable future. It is clear that in order to continue the financing required, our emphasis must be on performance for shareholders. During 1979, our common shareholders provided us with more than $57.2 million of additional equity capital, 2,959,506 additional shares, to help finance needed facilities. In return, our common shareholders earned $2.97 per share, up from $2.83 in 1978.

You, our shareholders, have taken long-term risks in order to ensure an adequate power supply. The rate structure simply must be such that the bottom line is enticing to shareholders. Stock must be selling above book value, and we will do everything reasonable to make that happen.

To our employees we say thanks for a dedicated decade; your innovation and individual energy have made our Company part of the solution to our country's problems. To our directors we again express appreciation for the widsom, stability and leadership you provide.

PNM enters the 1980's confident of its ability to provide reliable service and maintain the high level of accountability to its customers and to you, our shareholders.

Sincerely,

J.D. Geist

J. D. Geist
President

G. A. Schreiber

G. A. Schreiber
Chairman of the Board

Economic Picture

New Mexico Economy

PNM is situated in one of the growth areas of the Rocky Mountain West, as the Company's construction budget over the past decade indicates. Projections show that during 1979-1984 population in PNM's service area will grow by 16 percent, or an average of 2.9 percent per year. The national annual growth rate is expected to be about 1 percent. In contrast, the growth rate over 1974-1979 was 14.5 percent, an annual rate of 2.5 percent. The population in PNM's service area is currently estimated to be 532,000. Total state population is about 1,241,000.

Employment for the growing population in New Mexico is centered on government agencies plus trade and service businesses. Manufacturing represents a small portion of the economy with about 7 percent employment. This low percentage of manufacturing workers serves as insulation, tending to protect New Mexico from the effects of any national recession. The combined industrial segment of the economy (mining, manufacturing, and construction) provides about 20 percent of total employment.

But this industrial figure is climbing due to significant growth in coal and uranium mining. Besides the increasing development of huge coal reserves, the state currently supplies approximately 50 percent of the country's production of yellowcake. PNM supplies electricity to about 70 percent of the state's uranium mining activity.

In addition to the traditional segments of New Mexico's economy, there is also a large and active high technology research sector, including Los Alamos Scientific Laboratories and Sandia Laboratories. PNM is also recognized as a leader in energy research and development because of its work in projects such as solar and geothermal energy applications.

While the per capita income in New Mexico ranks in the bottom one-fifth of all states, the rate of increase is greater than most other states. Since 1974, personal income in New Mexico has been growing at one of the fastest rates in the Rocky Mountain region. Per capita income in the Albuquerque metro area, in which 80 percent of PNM's customers live, is currently about equal to the national average. The continuation of these trends is expected to lift New Mexico's per capita income above its current national ranking.

Construction and Financing

Nineteen seventy-nine was a significant year for PNM. The year represented the peak of our construction program in terms of annual dollars spent. In 1979, net utility plant additions totaled about $317 million, compared to about $199 million in 1978. Our current construction budget indicates a downward trend in annual construction dollars for the next several years until we begin our next major generating project. Also, the Company acquired full ownership of San Juan Unit 4 by purchasing Tucson Electric Power Company's 50 percent share of the unit. Construction of this 472-megawatt unit is scheduled for completion in 1982. The third unit at the San Juan Generating Station went into commercial service in December, bringing 240 net megawatts into the grid for PNM's customers.

New external funding for 1979 included a $40 million 8.75 percent preferred stock issue, an issue of common stock for $48 million, and $130 million in 6.5 percent pollution control revenue bonds. Common stock totaling $9.3 million was also raised through the Dividend Reinvestment Plan, the Employee Stock Purchase Plan, and the Tax Reduction Act Stock Ownership Plan (TRASOP). The Company also obtained commitments to place directly with institutional investors $45 million of 10⅛ percent first mortgage bonds, of which $17 million was received in 1979, with the remaining $28 million received in January 1980.

Revenues and Expenses

Revenues rose from $187 million in 1978 to $244 million in 1979, or 31 percent. This follows a 35 percent increase from 1977 to 1978. Of the $57 million increase in revenues, it is estimated that 26 percent resulted from increased kilowatt-hour sales, 26 percent from fuel clause adjustments and 48 percent from increases in base electric rates. Electric sales grew from about 4.5 billion to almost 5 billion kilowatt-hours, a 9.6 percent increase.

In 1979, fuel and purchased power expense was up by about 36 percent due to increased energy requirements and costs of fuel. Other operating and maintenance expenses climbed by 22 percent, compared to 26 percent in 1977-1978. Cost control programs were continued during the year and a trend toward improved cost-effectiveness is evident.

As a result of the financing for our construction program, interest expenses on short-term debt rose due to a higher level of borrowing and increases in the interest levels. Long-term debt also grew in 1979 and total interest charges were up by about $3.7 million. Preferred dividends increased by about $3.8 million.

Earnings

During 1979, PNM's net earnings available to common shares grew from about $29 million to $43 million, or about 47 percent. However, reflecting the Company's increased investment in plant, shares outstanding climbed from approximately 12.6 million shares to 15.6 million, or 23 percent. Earnings per share for 1979 were $2.97, compared to $2.83 for 1978, on average shares outstanding.

The increase in average shares outstanding was due to the sale of common stock in 1978 and 1979 to finance our construction program. Return on average common equity for 1979 was 13.6 percent, compared to 13 percent for 1978.

Rates and Regulation

As an electric and water utility operating in the State of New Mexico, PNM is subject to the jurisdiction of the New Mexico Public Service Commission (NMPSC). Activities of the Company regulated by the NMPSC include rates, quality of service, issuance of securities, and generation and transmission construction. The Federal Energy Regulatory Commission (FERC) has jurisdiction over rates charged by PNM for electricity sold to other electric utilities.

Since mid-1975, PNM has used a method of rate adjustment called Cost of Service Indexing, which allows recovery of present-day costs of generating and distributing electricity. As originally designed, the Index was applied to rates under jurisdiction of the NMPSC, and allowed a quarterly adjustment when return on average common equity fell below or exceeded a band of 13.5 to 14.5 percent.

In May of 1979, however, the NMPSC ruled that the rate adjustment method could serve its intent by allowing annual adjustments. At that time, the NMPSC allowed the "rolling-in" of the factor into the base rate charge and during the remainder of 1979 the Indexing factor was removed as a separate item. The NMPSC determined that PNM would be allowed to adjust rates in a manner designed to attain earnings of 13.5 percent on year-end common equity. The first annual Index factor was calculated on 1978 revenues and expenses, with certain adjustments. Investment in the construction work in progress relating to San Juan Unit 3, placed in service in late 1979, and all pollution control equipment at the San Juan Generating Station was included in the revised calculations. The allowance for funds used during construction rate on other construction work in progress was changed from 6.5 percent to 7.5 percent. A composite return on accumulated deferred investment tax credits was allowed. With the switch from quarterly to annual adjustment of the factor and with the additional procedural and reporting requirements, Indexing has become less automatic; however, it retains many advantages over a traditional rate filing, including significant reductions in traditional regulatory lag. The New Mexico Attorney General appealed the May 1979 Order to the Santa Fe District Court and is contending that the formula used by the NMPSC in arriving at the annual Index factor produces excessive revenues. The NMPSC and the Company are opposing the Attorney General's position.

On the basis of most measures of financial integrity, the Cost of Service Index has been successful to date. PNM's total capitalization more than tripled between 1974 and 1978, compared to an industry average increase of about 40 percent. Yet, during this period, PNM improved its position relative to the industry average. Return on average capital, return on equity, before and after tax interest coverages, and market price-to-book value ratio improved markedly. In particular, return on average common equity rose approximately 39 percent from 9.7 percent in 1974 to 13.6 percent in 1979.

As part of a review of the Indexing procedures, PNM filed a rate redesign package with the NMPSC on December 31, 1979, to assist the NMPSC in complying with the Public Utilities Regulatory Policies Act (PURPA). The federal law requires utility regulators nationally to review cost and price standards, to promote conservation by utility customers and to increase the efficiency of electric energy use.

If approved by the NMPSC, the Company's proposed rate redesign would promote energy conservation as well as provide rate incentives to high-use customers who shift electric consumption off-peak when generating costs are lowest. The proposal would offer high-use electric customers the possibility of being billed for electricity based on the times of the day and seasons the power is used. The concept, called Time-of-Day or Time-of-Use rates, currently is not available from any utility in New Mexico.

The Company has a fuel adjustment clause which allows the direct pass-through of increased fuel costs. The adjustment is applicable to all sales. An additional part of the proposed rate redesign filed with the NMPSC would allow the Company to "zero out" the fuel adjustment factor by rolling the factor into the base rate for electrical service.

Electric Operations

The power produced by PNM comes from generating facilities as shown in the following table:

Location and Generating Station	PNM's Share of Capacity (MW)
Coal-Fired Stations	
Near Farmington	
Four Corners Units 4 & 5	208
San Juan Units 1, 2, & 3	550
Gas- and Oil-Fired Stations	
Albuquerque	
Person Station	96
Reeves Station	175
Prager Station	22
Santa Fe	
Santa Fe Station	11
Las Vegas	
Las Vegas Turbine	20
TOTAL	1,082

The Company holds a 13 percent ownership in Units 4 and 5 of the Four Corners Generating Station, a 50 percent ownership in San Juan Station Units 1, 2, and 3, and 100 percent ownership of the gas- and oil-fired stations. The Prager, Santa Fe, and Las Vegas Stations are used primarily to meet peak loads.

In 1979 PNM's generating fuel was mostly coal, accounting for about 67 percent of total kilowatt-hours produced. Natural gas provided 31.5 percent and oil 1.5 percent. With the addition of 240 megawatts of coal-fired capacity from San Juan Unit 3 in December of 1979, PNM's forecasted generation requirements from coal will rise to 83 percent, with natural gas and oil providing 15.8 percent and 1.2 percent, respectively, in 1980.

PNM through its operating divisions provides electric service to about half the people living in New Mexico. The Albuquerque Division service area includes roughly a third of the population of the entire state. The Belen and Bernalillo Divisions serve the rapidly growing areas south and north of Albuquerque, respectively. The Santa Fe Division serves the State Capital and surrounding communities. The Las Vegas Division serves Las Vegas on the eastern slopes of the Sangre de Cristo Mountains in north-central New Mexico. The Deming Division service area lies in the extreme southern portion of the state, just north of the Mexican border. The Western Division serves a portion of the uranium and coal mining areas west of Albuquerque.

In addition to the operating divisions, PNM-generated electricity is purchased by several other utilities, both publicly and privately owned, for distribution to their customers within the state.

As a regulated business, PNM operates under franchise agreements. Municipal electric franchise expiration dates are as follows: Albuquerque — 1992, Belen — 1990, Bernalillo — 1998, Deming — 1993, Las Vegas — 1996, and Santa Fe — 1999.

Water Operations

Water service in Santa Fe and Las Vegas is also provided by PNM. The water facilities were acquired along with the Santa Fe and Las Vegas electric systems many years ago.

During the year, PNM reached agreement with the City of Santa Fe resulting in a new water franchise. Resolution of conflicting points of view expressed by the City, PNM, and Santa Fe County was gained by further expansion of the duties of the Metropolitan Water Board. In an area where water is a critical resource and a key to development, the Board will serve as a way for the three parties to combine their expertise and meet the long-term needs for all concerned.

In large part, the credit for the success of the negotiations which resulted in the franchise agreement belongs to the PNM employees in Santa Fe. Their abilities and persistence turned a difficult situation into one of cooperation for the long-term future of water supply in Santa Fe. The new water franchise for Santa Fe will be in effect until the year 2004. The water franchise for Las Vegas expires in 1993.

The Future

Construction and Financing

Capital expenditures in 1980 are expected to drop to about $299 million, the major portion of which is for the construction of the fourth generating unit at San Juan and the three units at the Palo Verde Nuclear Generating Station in Arizona. To provide funds for the 1980 construction program, your company anticipates that it will offer up to $50 million of preferred stock in April and approximately $60 million of common stock during the second half of the year. PNM also expects to raise approximately $14 million through its internal stock programs.

In addition to the January receipt of the $28 million from the private placement first mortgage bond transaction, the Company's current financing plan also includes a first mortgage issue of approximately $60 million during the second half of the year. Use of approximately $77 million of low-cost pollution control revenue bonds currently held in trust is planned. Funding requirements will also be provided for by continued use of short-term debt. Additionally, your Company plans to participate with the City of Farmington in the issue of $26 million in pollution control revenue bonds for environmental control structures at the Four Corners Generating Station.

PNM's planned construction program over the next five years is estimated to be $1,084 million. Of this amount, approximately $593 million is for generation-related construction, including nuclear fuel, land and water acquisitions, with an additional $187 million for environmental control systems. The majority of this money is for continuing construction at the San Juan Generating Station, the Palo Verde Nuclear Generating Station in Arizona, a large pumped storage project, and PNM's interest in additional pollution control equipment for the Four Corners Generating Station. The balance of the $1,084 million will be spent over the next five years on transmission and distribution systems plus additional operating facilities for both electric and water customers. Additionally, PNM's wholly owned subsidiary, Paragon Resources, Inc., has a five-year capital expenditure program of $48 million, with about $15 million in 1980, primarily for developments related to future generation projects.

Sales and Rate Activities

Total system requirements in 1980, including sales to wholesale customers, are projected to increase by 15.8 percent. Total peak demand is projected to grow by 15.4 percent. The forecasted peak demand for the summer of 1980 is 987 megawatts. To supply this peak demand and maintain an adequate reserve margin for contingencies, PNM has a total installed capacity of 1,082 megawatts (11 megawatts of which is scheduled for retirement in early 1980, subject to a current review) and has contractually arranged to purchase an additional 160 megawatts of capacity from other utilities plus a projected eight megawatts from load management for resource capacity of 1,239 megawatts.

During the fourth quarter of 1979, PNM and the Los Angeles Department of Water and Power completed negotiations for the sale of firm surplus energy from San Juan Station to Los Angeles. Final contracts, signed in January 1980, provide for the sale of 700,000 megawatt-hours until April 1982.

In January 1980, your Company completed contract negotiations with San Diego Gas and Electric Company for the sale of contingent capacity from San Juan Station. This delivery of energy is contingent on the availability of the four units at San Juan and Palo Verde Unit 1. The contract specifies the sale of 236 megawatts each year over a six-year period (a total of about 8.6 million megawatt-hours of energy) commencing with the in-service date of San Juan Unit 4, anticipated to be May 1982.

As a result of the purchase of Tucson Electric Power Company's share of San Juan Unit 4, and the contingent sale of power from this unit to San Diego Gas and Electric during 1982-1987, PNM has not only assured availability of electricity to its customers into the 1990's, but additionally has been able to accomplish this at capacity costs of the 1970's rather than the late 1980's. The savings to PNM's customers will be substantial.

According to the schedule set by the NMPSC, PNM has filed a new Cost of Service Indexing factor which will be collected subject to refund beginning on March 21, 1980, while the NMPSC decides the case. The factor reflects increased costs PNM experienced during 1979.

In the near future, PNM will submit revised rates to the Federal Energy Regulatory Commission for wholesale customers based on test year 1980 budgeted operating data. Final decisions in pending cases have not yet been issued; however, the rates have been put into effect subject to refund.

The Company and Its People

Employees are PNM's most important asset. The employees work together to provide customers not only with the reliable service they expect today, but employees also test and implement new ideas and plans for dependable service in the years ahead.

During 1979 PNM added 257 additional employees. Although the Company's continued growth accounted for some of the increase, it was growing regulatory and environmental requirements which accounted for much of the increase. Effective environmental performance requires that the Company constantly monitor power plant emissions and maintain the necessary pollution control equipment. Detailed environmental studies are now required to support the construction of new generation and transmission facilities. To encourage energy conservation and to meet the requirements of the Public Utilities Regulatory Policies Act, personnel were added to provide additional assistance to customers and prepare studies for submission to appropriate agencies. The continued effect of these various activities on the total number of employees was significant.

PNM continues its tradition of attracting very talented and highly skilled new employees necessary to keep pace with customer needs. Of the 2,311 employees, almost 850 craft personnel are represented by Local Union 611 of the International Brotherhood of Electrical Workers. The PNM-IBEW contract expires April 30, 1981.

Employee Development

A total of 1,730 employees participated in Company-sponsored training programs during the 12-month period. Additional programs assisting employees wishing to further their education and job skills at local schools and universities are also offered.

Employee Benefits

As part of a continuing effort to retain skilled and trained employees as well as to attract new personnel, benefits, including life, health, and dental insurance as well as retirement plans, have been upgraded. Employee wages during 1979 stayed within the President's salary guidelines with isolated exceptions receiving prior approval by the federal government.

Promotions and Management Changes

An expressed principle of the Company is to promote from within its own ranks whenever practical. As a company operating in a growth mode, many jobs become available. During 1979, 877 employees were promoted to positions of higher responsibility.

The Company's Board of Directors elected two employees to vice president positions and promoted a third employee to Treasurer in April of 1979.

P. J. Archibeck was promoted to Treasurer from his previous position as Assistant Treasurer.

T. P. Warnke was elected District Vice President of PNM's San Juan area. Mr. Warnke, a former manager of PNM's Deming Division, previously served as manager of the San Juan area.

J. L. Wilkins was elected Vice President of Engineering and Construction. A past chairman of the National Electric Reliability Council, Mr. Wilkins previously was group manager of engineering and construction.

Subsidiaries

PNM has an interest in two subsidiaries, Paragon Resources, Inc. (formerly Public Service Land Company) and Western Coal Co. Paragon Resources, Inc. is a wholly owned subsidiary, organized to secure water rights and property for the Company's various projects and business-related needs. Chief among these needs are plant sites and water for Company water systems and for cooling purposes at generating plants.

Western Coal Co. is jointly owned by PNM and Tucson Electric Power Company. The purpose of Western Coal Co. is to secure coal leases and provide fuel for San Juan Generating Station. The San Juan Generating Station has contracted with Western Coal Co. to supply all coal required for the life of the plant.

Research, Development and Demonstration

PNM is involved in a number of research, development, and demonstration projects designed to increase Company operating efficiency, expand knowledge in energy use and alternatives, and protect the environment.

- Because water resources are scarce in New Mexico, PNM is evaluating treatment procedures necessary for water to be recovered from uranium mining activities for use in generating station applications.

- PNM is investigating the economic recovery of deep seam Fruitland Formation coal at depths below strippable levels, using underground coal gasification technology.

- Numerous solar research projects are underway including the performance of both passive and active solar residential and commercial systems plus water heating applications. PNM is also participating with Western Energy Supply and Transmission Associates (WEST) in the nation's largest solar monitoring project which will provide an excellent data base for future solar projects.

- PNM is also studying the effect of transmission lines on birds of prey and their habitats. This nationally recognized study will be completed in early 1980.

- At San Juan, PNM is developing techniques for remote measurement of visible and invisible power plant plumes. This project is also funded by WEST. PNM is also testing the use of ceramic-lined pipe sections in an effort to find ways to increase abrasion resistance in coal-handling systems at San Juan.

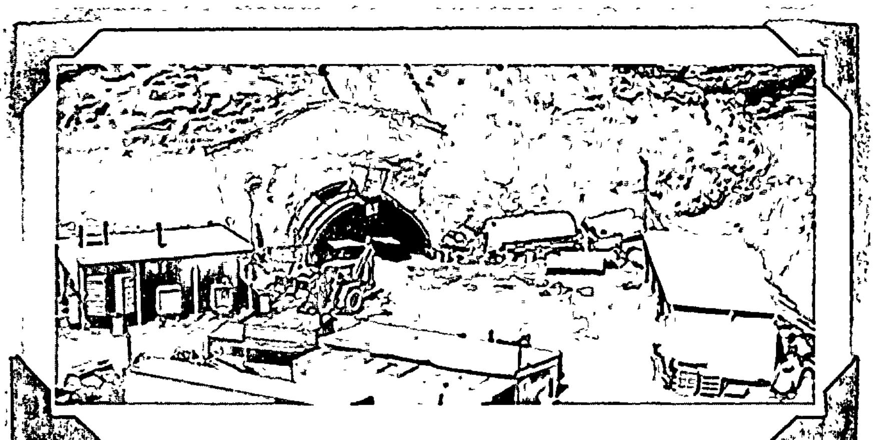
- An improved computer-assisted planning tool is being developed to enhance PNM engineers' ability to evaluate system distribution plans and alternatives.

- In the area of nonconventional electric generation, PNM, along with the Department of Energy and Union Oil Co., is constructing the nation's first hot water geothermal generating facility. When completed, this demonstration plant will produce 50 megawatts. Ultimately, the geothermal field could produce about 400 megawatts. The Company is also in the beginning phase of work on a pumped storage facility which, when completed in 1989, will produce about 600 megawatts.

- In 1980, Company load management engineers will join with private individuals in the Deming area to construct a vertical wind axis generator for use in irrigation and rural homes.

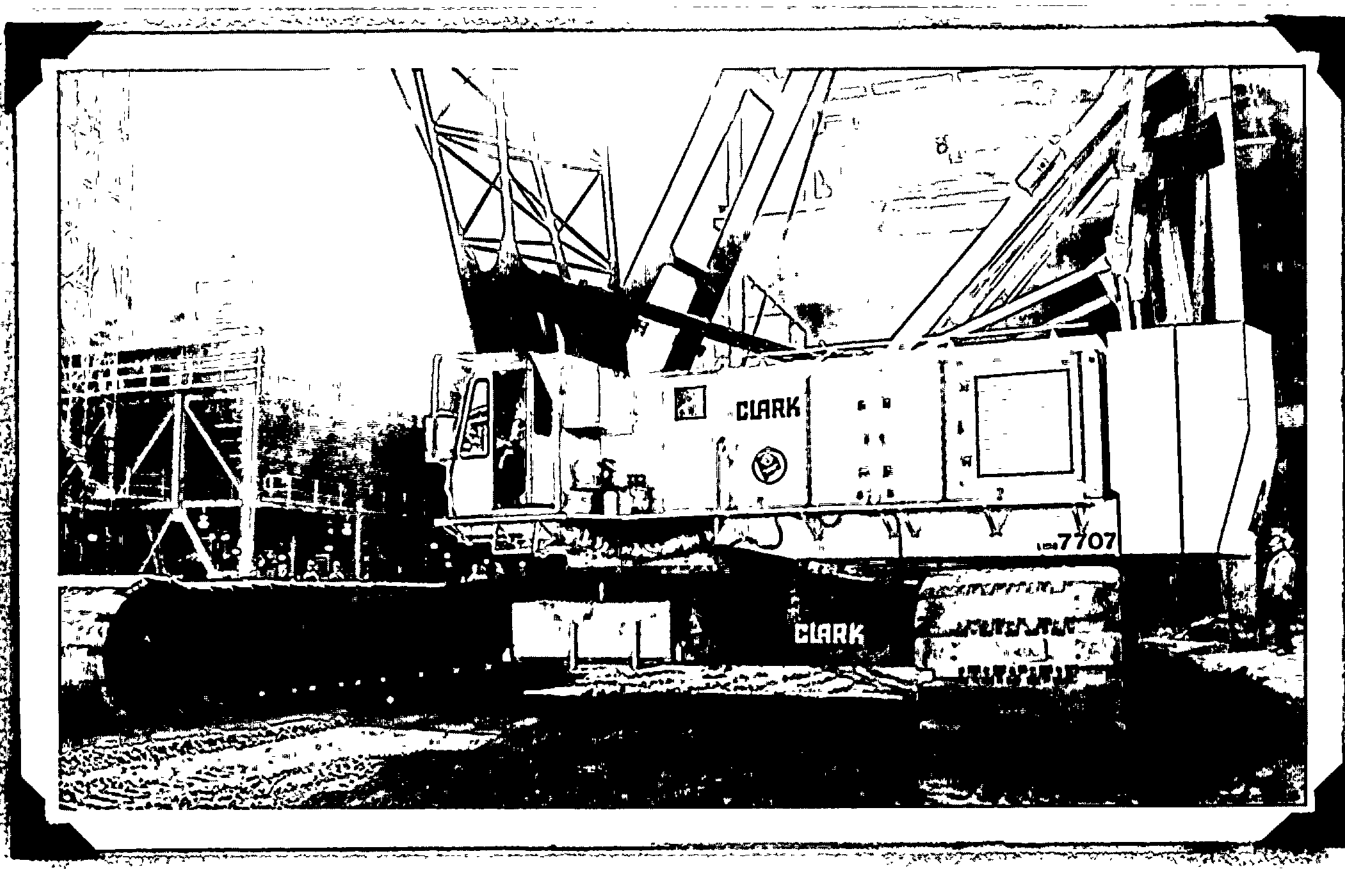
- Subsynchronous resonance, hardly a household word, is very important to utilities. The problem lies in vibrations created by transmission lines which can damage the power plant turbine-generator. PNM and ten other western utilities contracted with General Electric and Westinghouse in 1978 to develop a relay that could sense the vibrations and disconnect the generator before any damage could be done. As a result of this study, two relays were installed at the San Juan Generating Station in 1979 — the first of their kind in the country. Additional equipment is scheduled to be installed in 1980.

- Another major project during 1978 and 1979 was the High Silica Control Project. This involved experimentation with a new chemical to disperse silica in the water that normally collects as scale on heat transfer surfaces of power plant equipment, thereby reducing plant efficiency and causing the plant to use more water. The experiment carried out at Albuquerque's Person Generating Station resulted in saving one million gallons of water per day on just one unit.



A test tunnel has been completed for PNM's hydroelectric pumped storage project.

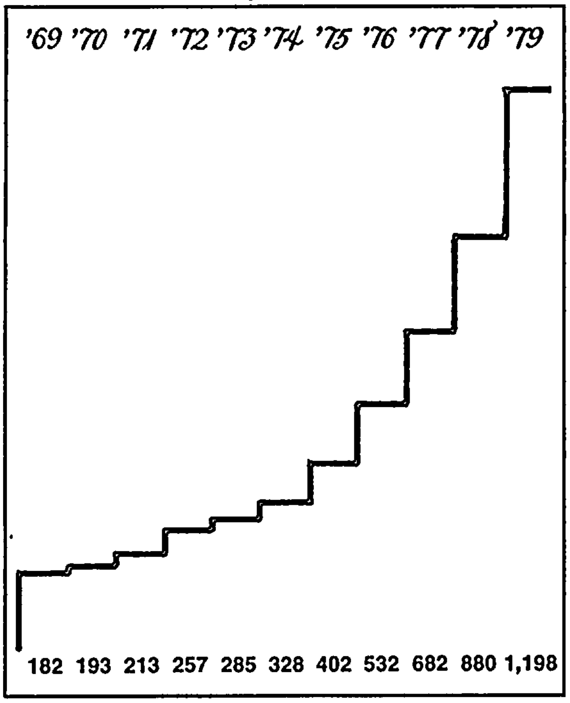
Index to Financial Data



With the completion of Unit 3 in 1979, construction now centers on San Juan Unit 4.

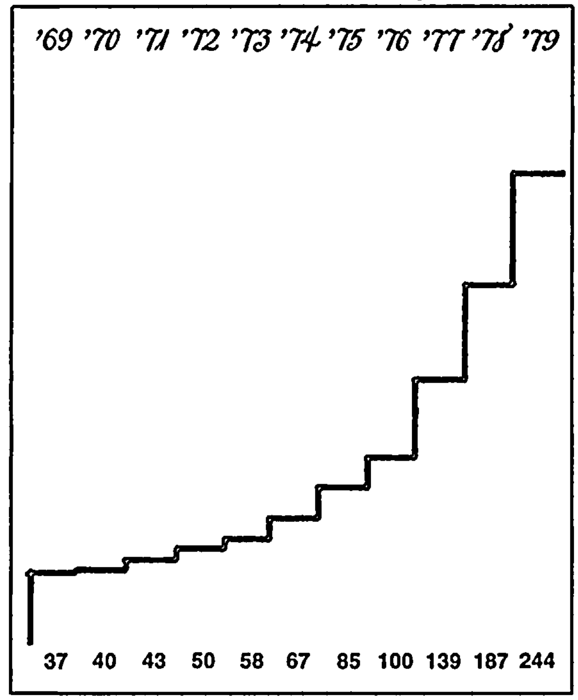
Growth Graphs

Gross Plant Investment



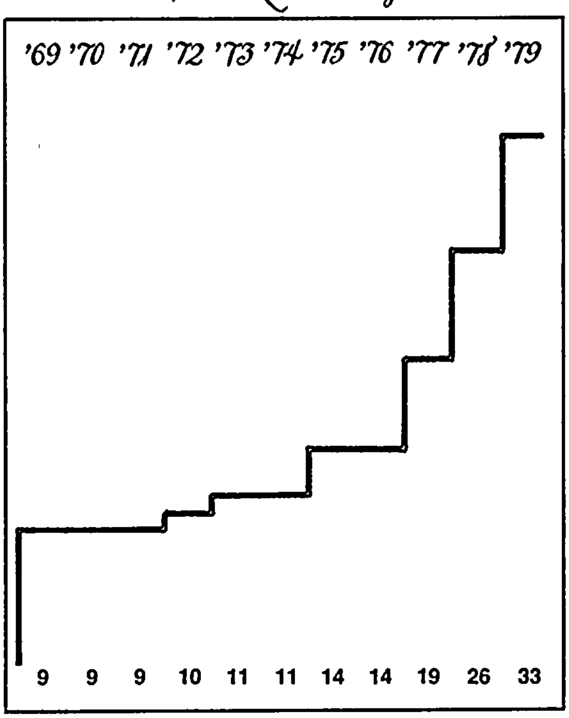
MILLIONS OF DOLLARS

Total Operating Revenues



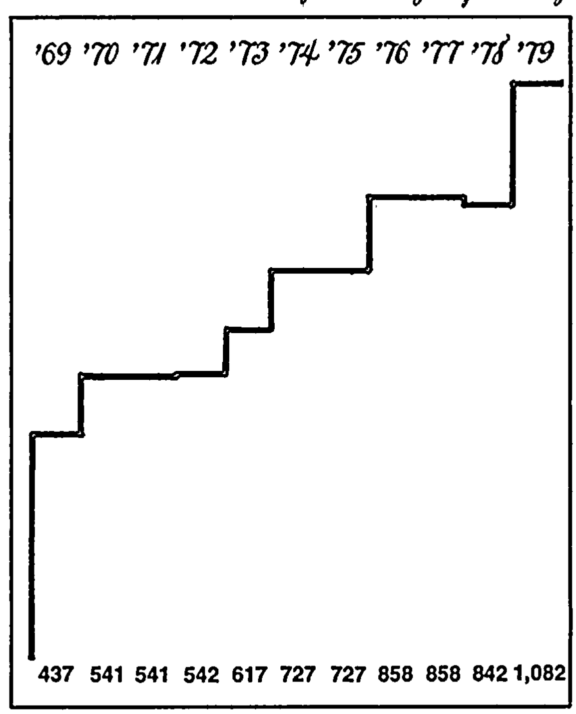
MILLIONS OF DOLLARS

Federal, State, Local and General Taxes



MILLIONS OF DOLLARS

Net Generating Capability



THOUSANDS OF KILOWATTS

Comparative Operating Statistics

	1979	1978	1977	1976
ELECTRIC SERVICE				
ENERGY SALES—kWhr (in thousands)				
Residential	1,067,755	1,000,564	957,390	916,748
Commercial	1,403,282	1,353,805	1,320,651	1,277,025
Industrial	858,533	797,314	686,845	605,559
Other ultimate customers	159,396	164,901	160,922	157,694
Total sales to ultimate customers	3,488,966	3,316,584	3,125,808	2,957,026
Sales for resale	1,471,485	1,211,242	1,241,195	638,207
Total energy sales	4,960,451	4,527,826	4,367,003	3,595,233
ELECTRIC REVENUES (in thousands)				
Residential	$ 66,262	$ 51,414	$ 39,547	$ 32,423
Commercial	77,806	60,125	45,520	36,198
Industrial	40,467	28,860	18,918	13,070
Other ultimate customers	8,704	7,052	5,215	4,168
Total revenue from ultimate customers	193,239	147,451	109,200	85,859
Sales for resale	44,000	32,568	23,219	9,340
Total revenue from energy sales	237,239	180,019	132,419	95,199
Miscellaneous electric revenues	2,532	2,581	2,605	1,935
Total electric revenue	$ 239,771	$ 182,600	$ 135,024	$ 97,134
CUSTOMERS AT YEAR END				
Residential	184,979	175,439	164,803	156,116
Commercial	20,334	19,496	18,374	17,483
Industrial	485	482	493	489
Other	264	263	265	250
Total ultimate customers	206,062	195,680	183,935	174,338
Sales for resale	5	5	5	5
Total customers	206,067	195,685	183,940	174,343
Reliable net capability — kW	1,082,000	842,000	858,000	858,000
Coincidental peak demand — kW	855,000	809,000	715,000	633,000
Average fuel cost per million BTU	120.72¢	105.52¢	92.74¢	61.83¢
BTU per kWhr of net generation	10,476	10,993	11,004	11,084
WATER SERVICE				
SALES — Gallons (in thousands)				
Customer sales	2,509,868	2,747,924	2,726,059	2,959,209
Interdepartmental sales	5,947	5,198	5,742	4,014
Total water sales	2,515,815	2,753,122	2,731,801	2,963,223
REVENUES (in thousands)				
Customer sales	$ 4,595	$ 4,599	$ 3,606	$ 2,386
Interdepartmental sales	4	6	6	3
Total water sales	$ 4,599	$ 4,605	$ 3,612	$ 2,389
Customers at year end	18,755	18,079	17,427	16,838

(1) Reclassified against expense

(2) Certain customers were reclassified from commercial to industrial during 1975. The reclassification accounted for a change of 220 customers in both categories.

1975	1974	1973	1972	1971	1970
875,361	828,243	786,108	706,973	648,626	583,136
1,177,953	1,128,576	1,110,147	985,431	885,782	792,376
530,188	549,622	616,405	653,761	618,695	552,118
136,136	137,843	128,171	123,568	116,202	107,598
2,719,638	2,644,284	2,640,831	2,469,733	2,269,305	2,035,228
578,037	250,901	122,656	114,333	106,000	98,026
3,297,675	2,895,185	2,763,487	2,584,066	2,375,305	2,133,254
$ 28,912	$ 23,314	$ 20,552	$ 17,760	$ 15,295	$ 13,910
30,851	25,403	22,283	19,421	16,309	14,784
9,993	8,349	7,210	7,229	6,549	5,963
3,361	3,004	2,613	2,204	1,994	2,056
73,117	60,070	52,658	46,614	40,147	36,713
8,241	2,782	1,074	937	857	778
81,358	62,852	53,732	47,551	41,004	37,491
1,412	2,406	2,803	795	670	621
$ 82,770	$ 65,258	$ 56,535	$ 48,346	$ 41,674	$ 38,112
151,111	147,516	143,201	136,515	127,911	120,865
16,738(2)	16,469	16,241	15,754	14,775	13,908
515(2)	298	295	303	308	300
246	231	229	221	205	201
168,610	164,514	159,966	152,793	143,199	135,274
4	4	3	3	3	3
168,614	164,518	159,969	152,796	143,202	135,277
727,000	727,000	617,000	542,000	540,700	540,700
586,000	583,400	533,000	491,700	458,700	400,600
47.23¢	39.49¢	26.16¢	24.47¢	23.55¢	23.04¢
10,848	11,054	11,017	10,841	10,870	11,058
2,859,783	3,013,508	2,855,673	2,781,854	2,563,745	2,564,580
9,195	12,568	10,710	3,638	1,707	1,782
2,868,978	3,026,076	2,866,383	2,785,492	2,565,452	2,566,362
$ 2,205	$ 2,103	$ 1,567	$ 1,530	$ 1,434	$ 1,418
3	6	3	(1)	1	1
$ 2,208	$ 2,109	$ 1,570	$ 1,530	$ 1,435	$ 1,419
16,437	16,158	15,848	15,454	15,024	14,495

Summary of Operations

	1979	1978	1977	1976	1975
	(In thousands except per share amounts)				
Total operating revenues	$244,370	$187,205	$138,636	$99,523	$84,978
Operating expenses:					
Operation and maintenance	134,539	103,864	76,524	51,535	39,785
Provision for depreciation and amortization	17,603	14,451	11,464	9,548	8,650
Taxes, other than income taxes	10,531	8,221	7,257	5,875	5,114
Income taxes	21,881	16,722	10,986	8,028	8,626
Total operating expenses	184,554	143,258	106,231	74,986	62,175
Operating income	59,816	43,947	32,405	24,537	22,803
Allowance for equity funds used during construction	15,594	10,541	6,218	4,109	1,583
Other income and deductions, net	2,401	2,257	1,435	689	530
Income before interest charges	77,811	56,745	40,058	29,335	24,916
Net interest charges	23,008	19,281	15,137	11,978	10,700
Net earnings	54,803	37,464	24,921	17,357	14,216
Preferred stock dividend requirements	12,196	8,384	6,285	4,194	2,952
Net earnings applicable to common stock	$ 42,607	$ 29,080	$ 18,636	$13,163	$11,264
Average number of shares outstanding	14,363	10,289	7,569	6,106	4,609
Per share amounts:					
Net earnings	$ 2.97	$ 2.83	$ 2.46	$ 2.16	$ 2.44
Dividends	$ 1.88	$ 1.72	$ 1.61	$ 1.42	$ 1.26

Management's Discussion and Analysis of the Summary of Operations

The following factors, which may not be indicative of future operations or earnings, have had a significant effect upon the Company's results of operations during the years 1978 and 1979.

Electric revenues increased $47.6 million in 1978 and $57.2 million in 1979. The principal factors causing these increases are as follows:

	1979	1978
	(In thousands)	
Increase in electric revenues due to:		
Increased kWhr sales (a)	$14,660	$ 4,584
Increased base rates (b)	27,597	29,912
Increased fuel cost adjustment factor (c)	14,963	13,104
	$57,220	$47,600

(a) kWhr sales—the number of customers increased in each period and the average use per customer decreased in 1978 but increased in 1979. Increases in kWhr sales were 3.7% in 1978 and 9.6% in 1979.

(b) Rate increases—the Company bills most customers under a Cost of Service Index order based upon the jurisdictional return on common equity. The Index order, formerly a quarterly adjustment, was revised to provide for annual adjustments to base rates effective May 15, 1979. The Company has periodically negotiated higher rates with certain customers whose rates are subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC). New rates for such customers were filed with the FERC and accounted for revenues, net of recorded provisions for possible refund, of $6.7 million in 1978 and $9.9 million in 1979 which are subject to refund pending a determination by the FERC. Accumulated revenues subject to refund, net of provisions for refund, at December 31, 1979 are $18.3 million.

(c) Fuel cost adjustment—natural gas fuel costs, cost of coal per ton and purchased power have accelerated rapidly. Such costs are passed on to customers.

Water revenues increased $1.0 million in 1978 as a result of rate increases allowed by the New Mexico Public Service Commission (Commission).

Operation and maintenance expenses increased $27.3 million in 1978 and $30.7 million in 1979. Principal causes are:

(a) Production of energy from the Company's own generating units decreased by 14.3% in 1978 but increased by 16.3% in 1979. A boiler explosion, causing the shutdown of the first unit at the San Juan Generating Plant in July 1977 and the return to service of the unit in May 1978, coupled with the purchase of lower cost energy on the interchange market rather than generating from the Company's gas and oil fired units, resulted in the Company being a net purchaser of 957 million kWhr in 1978. Although generation increased in 1979, the growth in kWhr sales resulted in the Company being a net purchaser of 752 million kWhr. Increased fuel and purchased power expenses resulting from the boiler explosion were $6.9 million for the entire period of the outage. Of such expenses $6.6 million were passed on to customers through the fuel adjustment clause by approval of the Commission and are subject to refund if it is determined that the Company was responsible for the explosion.

(b) Rapidly accelerating fuel costs.

(c) Higher cost of labor and related benefits due to higher wage rates and an increase in the number of employees necessary to operate the expanded electric generating and water facilities.

(d) General inflationary factors.

(e) Maintenance and repair expenses increased by $3.0 million in 1978 and $1.9 million in 1979. Overhauls and inspections at Person Station, the Four Corners plant and the San Juan plant accounted for increased costs of $2.4 million in 1978 and $1.3 million in 1979.

The Company's gross utility plant increased by approximately 29% in 1978 and 36% in 1979 as a result of expanded operations, the need to maintain reliable service and increasing environmental protection requirements. In addition, the Company purchased the fifty-percent undivided interest of Tucson Electric Power Company in San Juan Unit 4. This increase in utility plant and the Company's construction program have been the primary causes of increases experienced in the following areas of operations:

(a) Depreciation and amortization.

(b) Taxes, other than income taxes—increases in ad valorem taxes resulted from increased plant.

(c) Allowance for funds used during construction—increased construction at the San Juan plant and the Palo Verde Nuclear Generating Station.

(d) Interest charges and preferred stock dividend requirements—from 1977 through 1979 the Company issued $112 million principal amount of first mortgage bonds, utilized $147 million of proceeds of pollution control revenue bonds and issued $86 million of preferred stock, generally at higher rates than previous issues, and had up to $96 million principal amount of short-term debt outstanding.

Other income and deductions, net, increased $.8 million in 1978 primarily because the Company's share of earnings of its fifty-percent-owned subsidiary increased due to increased coal deliveries to the San Juan plant and an increase in the price per ton delivered.

As a result of items detailed above, earnings before income taxes, income taxes, net earnings and earnings per share of common stock all increased in 1978 and 1979.

Consolidated Balance Sheet

December 31, 1979 and 1978

Assets

	1979	1978
	(In thousands)	
Utility plant, at original cost (notes 4 and 8):		
Electric plant in service	$ 712,096	$462,621
Water plant in service	31,639	30,284
Common plant in service	17,340	14,148
	761,075	507,053
Less accumulated depreciation and amortization	127,939	102,033
	633,136	405,020
Construction work in progress	435,353	371,754
Electric plant held for future use	1,086	1,086
Net utility plant	1,069,575	777,860
Other property and investments:		
Non-utility property, at cost, net of accumulated depreciation of $757,000 in 1979 and $456,000 in 1978	17,362	9,516
Investment in fifty-percent-owned company	6,111	3,895
Other, at cost	1,875	1,747
Total other property and investments	25,348	15,158
Current assets:		
Cash (note 5)	3,810	1,929
Receivables:		
Customers	23,818	18,835
Other	13,809	18,231
Allowance for doubtful receivables	(224)	(106)
Fuel, materials and supplies, at average cost	22,073	16,015
Prepaid expenses	2,040	1,116
Deferred fuel costs	11,322	11,875
Total current assets	76,648	67,895
Deferred charges:		
Construction advance	—	17,037
Unamortized debt expense	6,918	5,364
Other deferred charges	7,957	5,433
Total deferred charges	14,875	27,834
	$1,186,446	$888,747

See accompanying notes to consolidated financial statements.

Capitalization and Liabilities

	1979	1978
	(In thousands)	
Capitalization:		
Common stock equity (note 2):		
Common stock of $5 par value. Authorized 20,000,000 shares; outstanding 15,601,739 shares in 1979 and 12,642,233 shares in 1978	$ 78,009	$ 63,211
Additional paid-in capital	185,600	145,433
Retained earnings	83,719	67,645
Total common stock equity	347,328	276,289
Cumulative preferred stock. Authorized 5,000,000 shares (note 3):		
Without mandatory redemption requirements. Outstanding 860,000 shares of $100 stated value and 800,000 shares of $25 stated value	106,000	106,000
With mandatory redemption requirements. Outstanding 400,000 shares of $100 stated value in 1979.	40,000	—
Long-term debt, less current maturities (notes 4 and 11)	431,655	356,347
Total capitalization	924,983	738,636
Current liabilities:		
Short-term debt (note 5)	95,960	23,805
Accounts payable	51,695	43,072
Preferred dividends declared	2,869	1,994
Current maturities of long-term debt (note 4)	5,224	1,189
Accrued interest	5,577	4,424
Accrued taxes	9,418	7,191
Other current liabilities.	4,220	4,226
Total current liabilities	174,963	85,901
Deferred credits:		
Customer advances for construction	7,180	5,603
Accumulated deferred investment tax credits (note 6)	47,896	36,224
Accumulated deferred income taxes (note 6)	22,529	17,980
Other deferred credits	8,895	4,403
Total deferred credits	86,500	64,210
Commitments and contingencies (notes 8, 9 and 10)		
	$1,186,446	$888,747

Consolidated Statement of Earnings

Years ended December 31, 1979 and 1978

	1979	1978
	(In thousands except per share amounts)	
Operating revenues:		
Electric (note 10)	$239,771	$182,600
Water	4,599	4,605
Total operating revenues	244,370	187,205
Operating expenses:		
Fuel and purchased power	85,143	62,694
Other operation expenses	34,351	28,002
Maintenance and repairs	15,045	13,168
Provision for depreciation and amortization	17,603	14,451
Taxes, other than income taxes	10,531	8,221
Income taxes (note 6)	21,881	16,722
Total operating expenses	184,554	143,258
Operating income	59,816	43,947
Other income and deductions:		
Allowance for equity funds used during construction	15,594	10,541
Equity in earnings of fifty-percent-owned company, net of taxes (note 6)	2,151	1,498
Other, net of taxes (note 6)	250	759
Net other income and deductions	17,995	12,798
Income before interest charges	77,811	56,745
Interest charges:		
Interest on long-term debt	24,236	21,349
Amortization of debt discount, expense and premium	394	347
Other interest charges	4,302	1,668
Allowance for borrowed funds used during construction	(5,924)	(4,083)
Net interest charges	23,008	19,281
Net earnings	54,803	37,464
Preferred stock dividend requirements	12,196	8,383
Net earnings applicable to common stock	$ 42,607	$ 29,081
Average number of shares outstanding	14,363	10,289
Per share amounts:		
Net earnings	$ 2.97	$ 2.83
Dividends	$ 1.88	$ 1.72

See accompanying notes to consolidated financial statements.

Consolidated Statement of Capitalization

Years ended December 31, 1979 and 1978

	1979	1978	Percentages 1979	Percentages 1978
	(In thousands)			
Common stock equity:				
Common stock:				
Balance at beginning of year	$ 63,211	$ 44,287		
Issuance of common stock	14,798	18,924		
Balance at end of year	78,009	63,211		
Additional paid-in capital:				
Balance at beginning of year	145,433	90,947		
Premium on common stock issued	42,466	57,241		
Expenses of stock issuance	(2,299)	(2,755)		
Balance at end of year	185,600	145,433		
Retained earnings:				
Balance at beginning of year	67,645	56,213		
Net earnings	54,803	37,464		
	122,448	93,677		
Cash dividends:				
Cumulative preferred stock	12,196	8,383		
Common stock	26,533	17,649		
	38,729	26,032		
Balance at end of year	83,719	67,645		
Total common stock equity	347,328	276,289	37.5%	37.4%
Cumulative preferred stock:				
Without mandatory redemption requirements:				
Balance at beginning of year	106,000	80,000		
Issuance of preferred stock	—	26,000		
Balance at end of year	106,000	106,000	11.5	14.4
With mandatory redemption requirements:				
Balance at beginning of year	—	—		
Issuance of preferred stock	40,000	—		
Balance at end of year	40,000	—	4.3	—
Long-term debt, less current maturities:				
Balance at beginning of year	356,347	244,721		
Addition to long-term debt	82,763	114,561		
Reduction of long-term debt	(6,544)	(2,305)		
Net change in unamortized discount and premium	(911)	(630)		
Balance at end of year	431,655	356,347	46.7	48.2
Total capitalization at end of year	$924,983	$738,636	100.0%	100.0%
Number of shares issued:				
$100 stated value cumulative preferred stock	400	260		
Common stock	2,960	3,785		

See accompanying notes to consolidated financial statements.

Consolidated Statement of Changes in Financial Position

Years ended December 31, 1979 and 1978

	1979	1978
	(In thousands)	
Funds provided:		
Net earnings	$ 54,803	$ 37,464
Charges (credits) to earnings not requiring funds:		
Depreciation and amortization	19,128	15,510
Provision for noncurrent deferred income taxes, net	4,549	1,149
Investment tax credit, net	11,672	10,378
Allowance for equity funds used during construction	(15,594)	(10,541)
Undistributed earnings of fifty-percent-owned company	(2,216)	(1,621)
Funds derived from operations	72,342	52,339
Sale of first mortgage bonds	17,000	65,000
Sale of cumulative preferred stock	40,000	26,000
Proceeds from pollution control revenue bonds	62,166	48,818
Sale of common stock	57,264	76,165
Proceeds from other long-term debt	3,597	743
Proceeds from short-term debt	290,315	142,280
Decrease in deferred charges	12,405	—
Utility plant retirements, net of removal costs	14,137	809
Decrease in working capital other than short-term debt	8,154	—
Other	6,113	4,086
	$583,493	$416,240
Funds used:		
Cash dividends	$ 38,729	$ 26,032
Utility plant additions	308,526	189,307
Payment of short-term debt	218,160	168,475
Reduction of long-term debt	6,544	2,305
Additions to non-utility property	8,157	—
Increase in deferred charges	—	22,316
Increase in working capital other than short-term debt	—	4,400
Other	3,377	3,405
	$583,493	$416,240
Changes in working capital other than short-term debt:		
Cash	$ 1,881	$ (3,708)
Receivables	443	15,140
Fuel, materials and supplies	6,058	1,801
Prepaid expenses	924	(115)
Deferred fuel costs	(553)	4,747
Accounts payable	(8,623)	(9,877)
Preferred dividends declared	(875)	(572)
Current maturities of long-term debt	(4,035)	176
Accrued interest	(1,153)	(832)
Accrued taxes	(2,227)	(3,035)
Other current liabilities	6	675
Increase (decrease) in working capital other than short-term debt	$ (8,154)	$ 4,400

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

December 31, 1979 and 1978

(1) Summary of Significant Accounting Policies

System of Accounts —

The Company maintains its accounting records in accordance with the uniform system of accounts prescribed by the Federal Energy Regulatory Commission (FERC) and adopted by the New Mexico Public Service Commission (Commission). As a result of the rate-making process, the application of generally accepted accounting principles by the Company differs in certain respects from the application by nonregulated businesses. Such differences generally regard the time at which certain items enter into the determination of net earnings in order to follow the principle of matching costs and revenues.

Principles of Consolidation —

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Paragon Resources, Inc. (formerly Public Service Land Company). All significant intercompany transactions have been eliminated.

Utility Plant —

Utility plant is stated at original cost, which includes payroll-related costs such as taxes, pensions and other fringe benefits, administrative costs and an allowance for funds used during construction. Contributions received from customers to meet the customers' special construction requirements are credited to utility plant.

It is Company policy to charge repairs and minor replacements of property to maintenance expense and to charge major replacements to utility plant. Gains or losses resulting from retirements or other dispositions of operating property in the normal course of business are credited or charged to the accumulated provision for depreciation.

Allowance for Funds Used During Construction (AFUDC) —

In accordance with the uniform system of accounts, AFUDC, a noncash income item, is charged to utility plant. The Commission ordered that AFUDC be limited to generating plant construction, effective April 22, 1975. The Commission further ordered, effective May 15, 1979, that the rate be increased from the previously approved 6.5% to 7.5% and allowed the Company to eliminate the recording of AFUDC on Unit 3 at the San Juan Generating Station and on pollution control plant associated with all San Juan units. The allowance for equity funds used during construction is credited to other income and deductions and the allowance for borrowed funds used during construction is credited to interest charges. The allocation of AFUDC between borrowed funds, after taxes, and equity funds is based on the method required by FERC.

Depreciation —

Provision for depreciation of utility plant is made at annual straight-line rates approved by the Commission. The average depreciation rates used were as follows:

	1979	1978
Electric plant	3.62%	3.39%
Water plant	1.88%	1.89%
Common plant	7.13%	5.89%

The provision for depreciation and amortization of certain equipment, including amortization applicable to capital leases, is charged to clearing accounts along with other costs of operation and subsequently apportioned to operating expenses and property accounts based on the use of the equipment. Depreciation of non-utility property is computed on the straight-line method.

Investment in Fifty-Percent-Owned Company —

The Company's investment in a fifty-percent-owned company is stated at equity. The co-owner, Tucson Electric Power Company, is participating with the Company in the construction and operation of a steam turbo-electric generating plant described in note (8). The generating plant utilizes coal from properties of the fifty-percent-owned company as a source of fuel.

Deferred Fuel Costs —

The Company uses the deferred method of accounting for the portion of fuel costs which is recoverable in subsequent periods under fuel adjustment clauses.

Amortization of Debt Discount, Expense and Premium —

Discount, expense and premium incurred in the issuance of the presently outstanding debt are being amortized by charges to income over the lives of the respective issues on the debt outstanding method.

Investment Tax Credits —

The Company follows the practice of deferring investment tax credits and amortizes them over the estimated useful lives of the related properties. Investment tax credit carryforwards are recorded to the extent of the sum of the investment tax credits which would have been realized if taxes payable had been based on pretax accounting income adjusted for permanent differences and the existing net deferred tax credits which would reverse during the investment tax credit carryforward period.

Income Taxes —

Certain revenue and expense items in the Consolidated Statement of Earnings are recorded in a year different from the year in which they are recorded for income tax purposes. Deferred income taxes are provided on these timing differences to the extent allowed for rate-making purposes. This normalization method is used primarily for differences attributable to deferred fuel costs, the use of liberalized depreciation methods and different lives under the asset depreciation range (ADR) than under the guideline depreciation provisions. Certain other differences result in a reduction in income tax expense in the current year. This flow-through method is used primarily for differences between tax depreciation computed under the guideline life provisions and book depreciation and certain capitalized construction costs, principally AFUDC, deducted currently for income tax purposes.

At present, rates applicable to certain customers subject to FERC control allow recovery of amounts necessary to provide additional tax normalization of the items described above which are accounted for under the flow-through method for other customers. Provision has been made for additional deferred income taxes attributable to amounts collected under these rates.

Revenues —

Revenues are recognized based on cycle billings rendered to customers monthly. The Company does not accrue revenues for services provided but not billed at the end of a fiscal period.

Pension Plan —

The Company's policy is to fund pension costs which are composed of normal costs and amortization of prior service costs over thirty years.

(2) Common Stock Equity

The Board of Directors reserved 2,000,000 shares of unissued common stock for the dividend reinvestment program, the Employee Stock Purchase Plan and the Tax Reduction Act Stock Ownership Plan, of which 1,229,413 shares remained unissued at December 31, 1979.

Charter provisions relating to the cumulative preferred stock and the indenture securing the first mortgage bonds impose certain restrictions upon the payment of cash dividends on common stock of the Company. At December 31, 1979, there were no retained earnings restricted under such provision.

(3) Cumulative Preferred Stock

The cumulative preferred stock may be redeemed by the Company, upon thirty days notice thereof, at stated redemption prices (plus accrued and unpaid dividends). Information concerning the cumulative preferred stock is as follows:

Series	*Stated Value*	*Shares Outstanding*	*Aggregate Stated Value (In thousands)*	*Stated Redemption Price* (a)
Without mandatory redemption requirements:				
1965 Series, 4.58%	$100	130,000	$ 13,000	$102.516
1974 Series, 9.2%	100	170,000	17,000	107.00
1975 Series, 10.12% (b)	100	100,000	10,000	110.12
9.16% Series (b)	25	800,000	20,000	27.29
8.48% Series (b)	100	200,000	20,000	108.48
8.80% Series (b)	100	260,000	26,000	108.80
		1,660,000	$106,000	
With mandatory redemption requirements:				
8.75% Series (b) (c)	100	400,000	$ 40,000	108.75

(a) Redemption prices are at reduced premiums in future years.

(b) Redemption may not be made through certain refunding operations prior to March 15, 1980 for the 1975 Series, or prior to June 1, 1981 for the 9.16% Series, or prior to April 1, 1982 for the 8.48% Series, or prior to April 1, 1983 for the 8.80% Series, or prior to February 1, 1984 for the 8.75% Series.

(c) On February 1, 1984 and on each February 1 thereafter, the Company shall redeem 13,000 shares of the 8.75% Series, pursuant to a mandatory sinking fund at a redemption price of $100 per share plus accrued and unpaid dividends.

(4) Long-Term Debt

The details of the Company's outstanding long-term debt including unamortized discount and premium, less current maturities, are as follows:

Issue and Maturity	*Interest Rates*	*1979*	*1978*
		(In thousands)	
First Mortgage Bonds:			
1980 through 1984	3 % to 3⅝%	$ 5,241	$ 9,012
1985 through 1989	4⅜%	8,580	8,690
1990 through 1994	4⅞%	9,880	10,002
1995 through 1999	5⅞% to 7¼%	32,197	32,602
2000 through 2004	7½% to 10⅛%	55,031	38,532
2005 through 2009	8⅛% to 9⅛%	119,073	119,290
2004 through 2009 — pollution control series, securing pollution control revenue bonds	6 % to 6⅞%	274,061	145,000
Funds held by trustee		(153,660)	(85,825)
Total first mortgage bonds		350,403	277,303
Pollution control revenue bonds, due 1984	5 % to 7.6%	77,000	77,000
Other		4,252	2,044
Total long-term debt		$431,655	$356,347

Substantially all utility plant is pledged to secure the first mortgage bonds.

Approximately 25 percent of the original principal amount of each series of first mortgage bonds will be redeemed through sinking fund requirements prior to the aforementioned due dates. The aggregate amounts (in thousands) of maturities on long-term debt outstanding at December 31, 1979 are as follows:

1980	$5,224
1981	2,314
1982	5,508
1983	2,816
1984	4,914

In August 1977 the City of Farmington, New Mexico issued and sold $77,045,000 principal amount of its 5.9% Pollution Control Revenue Refunding Bonds, Series 1977, the proceeds of which are expected to be used to retire 7.6% Pollution Control Revenue Bonds and 5% Pollution Control Revenue Bonds at their maturity in 1984. From and after such retirement, but not before, the Refunding Bonds will be payable out of revenues received by the City from the Company. Upon such retirement the Company will also guarantee the payment of the Series 1977 Bonds and secure its guaranty with an equal principal amount of its first mortgage bonds.

(5) Short-Term Debt and Compensating Balance Arrangements

The Company's interim financing requirements are met through issuance of unsecured notes payable to banks and commercial paper. The Company has agreed to maintain compensating balances with certain lending banks or to pay fees in lieu of such balances. Compensating balances are generally equal to 20% of the outstanding indebtedness or 10% of the lines of credit at such banks, whichever is greater. Details of the Company's short-term debt at December 31, 1979 and December 31, 1978 and for the years then ended were as follows:

	1979	1978
	(In thousands)	
Aggregate short-term debt outstanding:		
Notes payable to banks	$37,250	$ 4,050
Commercial paper	$58,710	$19,755
Average interest rate on outstanding debt:		
Notes payable to banks	14¾%	11¼%
Commercial paper	13⅜%	10⅛%
Maximum short-term debt outstanding during year	$95,960	$68,600
Average short-term debt outstanding during year	$38,460	$23,028
Weighted average interest rate on short-term debt outstanding during year, computed using daily outstanding balances:		
Stated interest rates	11⅞%	7¾%
Effective rate considering the effect of compensating balances and fees in lieu thereof	12⅞%	8⅛%
Unused lines of credit (subject to cancellation at the banks' option)	$60,140	$53,120
Compensating balances at end of year	$ 1,956	$ 916

Compensating balances have been reduced by the average difference between collected bank balances and book balances.

(6) Income Taxes

Income taxes consist of the following components:

	1979	1978
	(In thousands)	
Current Federal income tax	$ 3,864	$ 1,609
Current state income tax	1,467	1,048
Deferred Federal income tax	3,583	2,130
Deferred state income tax	677	657
Amount equivalent to current investment tax credit	13,611	12,413
Amortization of accumulated investment tax credit	(742)	(527)
Total income taxes	$22,460	$17,330
Charged to operating expenses	$21,881	$16,722
Charged to other income and deductions	579	608
Total income taxes	$22,460	$17,330

The Company has investment tax credit carryforwards, for tax purposes, of approximately $56,000,000 as of December 31, 1979 which will expire in 1985 and 1986. Of this amount, approximately $17,075,000 has been recorded, for financial statement purposes, as a reduction of deferred Federal income tax credits.

Deferred income taxes result from timing differences in the recognition of income and expenses for tax and accounting purposes. The major sources of these differences and the tax effects of each were as follows:

	1979	1978
	(In thousands)	
Deferred fuel costs	$ (495)	$ 2,396
Liberalized depreciation methods and asset class lives shorter than guideline lives	8,049	4,376
Other miscellaneous items	662	47
Investment tax credit carryforward	(3,956)	(4,032)
	$ 4,260	$ 2,787

The current portion of deferred income taxes (included in accrued taxes) results from timing differences on deferred fuel costs. Such balances amounted to $1,688,000 as of December 31, 1979 and $1,977,000 as of December 31, 1978 after reduction for investment tax credit carryforwards.

The Company's effective income tax rate was less than the Federal income tax statutory rate for each of the years shown. The differences are attributable to the following factors:

	1979	1978
Federal income tax statutory rate	46.0%	48.0%
Tax depreciation in excess of book depreciation caused by use of guideline depreciation provisions	(2.7%)	(1.2%)
Allowance for funds used during construction, net of depreciation adjustments	(12.1%)	(12.3%)
Certain employee benefits and taxes capitalized for financial statements, net of depreciation adjustments	(.5%)	(.7%)
Amortization of investment tax credits	(1.0%)	(1.0%)
Other miscellaneous items	(.6%)	(1.2%)
Company's effective income tax rate	29.1%	31.6%

(7) Pension Plan

The Company has a pension plan covering substantially all of its employees, including officers. The plan provides for monthly pension payments to participating employees upon their attaining the age of 65 or the age of 62 with 30 years service, the amount of such payments being dependent upon length of service and the average wage of the five most highly compensated consecutive years of employment. Early retirement is optional after age 55 or 30 years of service. Normal retirement benefits are the lesser of 65% of the participant's average annual base earnings rate minus $1,320 or 2% of the participant's average annual base earnings rate times his years of credited service. The Company made contributions to the employees' pension plan of $3,058,000 in 1979 and $2,807,000 in 1978 including normal costs and amortization of prior service costs.

Prior to May 1, 1978, the employees contributed $3 for the first $400 of monthly base salary, plus 3 percent of that part of base salary in excess of $400 during each month. The Company's funding of this portion of pension costs after such date did not have a significant effect on net earnings.

As of January 1, 1978, the most recent valuation date, the actuarially computed present value of vested benefits did not exceed the total market value of the pension fund assets and the estimated amount of the unfunded prior service liability was approximately $3,400,000.

(8) Construction Program and Jointly-Owned Plants

The Company is participating with Tucson Electric Power Company in the construction of the steam turbo-electric San Juan Generating Station. The Company owns an undivided fifty-percent interest in the first three units of the station. The Company purchased Tucson's fifty-percent undivided interest in the fourth and final unit of the San Juan Station in 1979 and now owns all of such unit.

The Company is also participating with several other utilities in the construction of the Palo Verde Nuclear Generating Station with the first unit scheduled for completion in 1983.

It is estimated that the Company's construction expenditures for 1980 will approximate $299,000,000 including expenditures on the jointly-owned projects. In connection, therewith, substantial commitments have been made. In addition to such amount, the Company's wholly-owned subsidiary forecasts construction expenditures of approximately $15,000,000.

Details of the Company's interest in jointly-owned plants at December 31, 1979 are as follows:

	Plant in Service	Accumulated Depreciation (In thousands)	Construction Work in Progress	Share of Total Plant
San Juan Generating Station	$388,893	$26,788	$208,063	65 %
Palo Verde Nuclear Generating Station	—	—	$170,159	10.2%
Four Corners Generating Station Units 4 and 5	$ 26,019	$ 6,440	$ 6,087	13 %

These amounts represent the Company's share of capital costs and the Company has provided its own financing. The Company's share of direct expenses is included in the corresponding operating expenses in the Consolidated Statement of Earnings. The Company also has undivided interests in transmission facilities which are not significant.

(9) Lease Commitments

The Company leases data processing, communication, office and other equipment, office space, utility poles (joint use) and real estate. Certain leases, primarily for data processing equipment, are capital leases. All other leases are operating leases.

Certain leases provide purchase options in the approximate amount of $2,146,000 for data processing equipment and $423,000 for construction equipment. Renewal options and contingent rental provisions were not significant.

Leased property under capital leases at December 31, 1979 and 1978 is as follows:

	1979	1978
	(In thousands)	
Data processing equipment	$3,871	$2,310
Other	232	181
	4,103	2,491
Less accumulated amortization	1,550	970
	$2,553	$1,521

Future minimum lease payments (in thousands) under capital leases at December 31, 1979 are:

1980	$ 922
1981	927
1982	812
1983	320
1984	230
Later years	457
Total minimum lease payments	3,668
Less amount representing executory costs	142
Net minimum lease payments	3,526
Less amount representing interest	770
Present value of net minimum lease payments	$2,756

Future minimum rental payments (in thousands) required under operating leases that have initial or remaining noncancellable lease terms in excess of one year as of December 31, 1979 are:

1980	$ 670
1981	351
1982	192
1983	147
1984	146
Later years	356
Total minimum payments required	$1,862

Rents charged to operating expenses were $1,277,000 in 1979 and $1,091,000 in 1978. Such amounts exclude payments made on capital leases. Rents charged to utility plant were $236,000 in 1979 and $577,000 in 1978.

The Company has entered into an agreement, not included above, for the lease of an office building currently under construction. Lease payments will commence after construction is completed in late 1980 at a rate of 4.42% of construction cost per year for the first three years and at 9.62% per year for the remaining thirty-two years of the initial lease term. Construction costs covered by the lease are projected to be approximately $18,700,000. Such lease is an operating lease.

(10) Revenues Subject to Refund

A boiler explosion caused the shutdown of Unit 2 at the San Juan Generating Station during the period July 1977 to May 1978. The major part of increased costs for replacement energy required during the shutdown was, with the approval of the Commission, initially passed on to customers through the fuel adjustment clause; however, the Commission subsequently ruled that charges for such increased costs are subject to refund if it is determined that the Company was responsible for the explosion. Amounts collected subject to refund, based upon a formula proposed to the Commission, were approximately $2.1 million in 1978 and $4.5 million in 1977. Based on the Company's investigation the Company is of the opinion that no refunds will be due. The Company's insurance covered a major portion of the cost of replacement.

In addition, the Company has collected certain revenues and has established a provision for possible refund of a portion of those revenues that have been collected subject to refund under wholesale rate cases filed with the FERC. Information concerning such revenues and provision is as follows:

	Revenues Collected	*Provision for Possible Refund*	*Net*
		(In thousands)	
1977	$ 1,705	$ —	$ 1,705
1978	6,678	—	6,678
1979	13,177	3,292	9,885
Total	$21,560	$3,292	$18,268

(11) Subsequent Event

On October 1, 1979 the Company entered into an agreement with a group of private investors to sell $45 million principal amount of 10⅛% first mortgage bonds due 2004. On October 24, 1979 the Company received $17 million principal amount of such issue with the balance of $28 million received on January 28, 1980.

(12) Quarterly Results of Operations (Unaudited)

The results of operations (in thousands except per share amounts) by quarters for 1979 and 1978 are as follows:

Quarter Ended	*Total Operating Revenues*	*Operating Income*	*Net Earnings*	*Net Earnings per Share*
December 31, 1979	$64,335	$16,378	$16,623	$.87
September 30, 1979	$66,725	$18,998	$16,661	$.88
June 30, 1979	$56,475	$13,192	$11,504	$.61
March 31, 1979	$56,835	$11,248	$10,015	$.57(a)
December 31, 1978	$49,473	$ 9,548	$ 7,781	$.45
September 30, 1978	$50,643	$13,039	$11,725	$.90
June 30, 1978	$44,079	$11,148	$10,005	$.84
March 31, 1978	$43,010	$10,212	$ 7,953	$.71

(a) In June 1979, the Company established a provision for possible refund on certain revenues collected subject to refund since October 1977. The effect of such provision was to reduce operating revenues, net earnings and net earnings per share by approximately $1.9 million, $1.3 million and $.10, respectively, for the first quarter of 1979. The quarterly results of operations have been restated accordingly.

In the opinion of management of the Company, all adjustments (consisting of normal recurring accruals) necessary for a fair statement of the results of operations for such periods have been included.

Certified Public Accountants

Suite 500 First Plaza
Post Office Box 1027
Albuquerque, New Mexico 87103

Peat, Marwick, Mitchell & Co.

The Board of Directors and Stockholders
Public Service Company of New Mexico:

We have examined the consolidated balance sheet of Public Service Company of New Mexico and subsidiary as of December 31, 1979 and 1978 and the related consolidated statements of earnings, capitalization and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Public Service Company of New Mexico and subsidiary at December 31, 1979 and 1978 and the results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

February 19, 1980

Stock/Dividend Data

Common Stock:

Range of sales prices of the Company's common stock, on the New York Stock Exchange (Symbol: PNM), and dividends paid on common stock for fiscal 1979 and 1978, by quarters, are as follows:

	Range of Sales Prices		Dividends
	High	Low	Per Share
Fourth Quarter, 1979	20¼	17½	$0.48
Third Quarter, 1979	21½	17⅜	0.48
Second Quarter, 1979	21¼	19	0.48
First Quarter, 1979	20⅝	19⅛	0.44
Fiscal Year	21½	17⅜	$1.88
Fourth Quarter, 1978	20½	18⅜	$0.44
Third Quarter, 1978	21¾	19⅝	0.44
Second Quarter, 1978	21⅛	19¼	0.42
First Quarter, 1978	21⅝	19⅜	0.42
Fiscal Year	21¾	18⅜	$1.72

Cumulative Preferred Stock:

While isolated sales of the Company's preferred stock have occurred in the past, the Company is not aware of any active trading market for its preferred stock.

Quarterly cash dividends were paid on each series of the Company's preferred stock at their stated rates during 1978 and 1979.

Supplementary Information on Changing Prices

The following supplementary information is supplied in accordance with the requirements of Financial Accounting Standards Board (FASB) Statement No. 33, Financial Reporting and Changing Prices, for the purpose of providing certain information about the effects of changing prices. It should be viewed as an estimate of the approximate effect of inflation, rather than as a precise measure.

Constant dollar amounts represent historical costs stated in terms of dollars of equal purchasing power, as measured by the average Consumer Price Index for All Urban Consumers (CPI-U). Current cost amounts reflect the changes in specific prices of plant from the date the plant was acquired to the present, and differ from constant dollar amounts to the extent that specific prices have increased more or less rapidly than prices in general.

The current cost of property, plant and equipment, which includes land, land rights, intangible plant, property held for future use and construction work in progress, represents the estimated cost of replacing existing plant assets and was determined by indices provided by an independent appraisal firm. These indices consist of a combination of the Handy-Whitman Index of Public Utility Construction Costs and special indices derived from actual appraisals of certain property, plant and equipment.

The accumulated provision for depreciation and amortization on the constant dollar and current cost amounts of property, plant and equipment was determined by calculating the ratio of the actual reserve to historical cost for each plant account and applying this ratio to the indexed amounts. The current year's provision for depreciation and amortization on the constant dollar and current cost amounts was determined by applying the Company's average annual depreciation and amortization rates for each plant account to the indexed amounts.

Fuel inventories, the cost of fuel used in generation, and power purchased for resale have not been restated from their historical cost. Regulation limits the recovery of fuel and purchased power through the operation of adjustment clauses or adjustments in basic rate schedules to actual costs. For this reason fuel inventories are effectively monetary assets.

As prescribed in Statement No. 33, income taxes were not adjusted. Accumulated Deferred Investment Tax Credits is treated as a monetary item, since it is returned to customers through adjustments in rates.

Under the rate making prescribed by the regulatory commissions to which the Company is subject, only the historical cost of plant is recoverable in revenues as depreciation. Therefore, the excess of the cost of plant stated in terms of constant dollars or current cost over the historical cost of plant is not presently recoverable in rates as depreciation, and is reflected as a reduction to net recoverable cost. While the rate-making process gives no recognition to the current cost of replacing property, plant and equipment, based on past practices, the Company believes it will be allowed to earn on the increased cost of its net investment when replacement of facilities actually occurs.

To properly reflect the economics of rate regulation in the Statement of Earnings from Continuing Operations, the reduction of net property, plant and equipment should be offset by the gain from the decline in purchasing power of net amounts owed. During a period of inflation, holders of monetary assets suffer a loss of general purchasing power while holders of monetary liabilities experience a gain. The gain from the decline in purchasing power of net amounts owed is primarily attributable to the substantial amount of debt which has been used to finance property, plant and equipment. Since the depreciation on this plant is limited to the recovery of historical costs, the Company does not have the opportunity to realize a holding gain on debt and is limited to recovery only of the embedded cost of debt capital.

Statement of Earnings from Continuing Operations Adjusted for Changing Prices

Year Ended December 31, 1979

	As Reported in the Primary Statement	*Adjusted for General Inflation (Constant Dollars)*	*Adjusted for Changes in Specific Prices (Current Cost)*
		(In thousands)	
Operating revenues	$244,370	$ 244,370	$ 244,370
Fuel and purchased power	85,143	85,143	85,143
Other operation expenses	34,351	34,351	34,351
Maintenance and repairs	15,045	15,045	15,045
Depreciation and amortization	17,603	27,364	28,666
Taxes, other than income taxes	10,531	10,531	10,531
Income taxes	22,460	22,460	22,460
Interest charges	23,008	23,008	23,008
Other income and deductions — net	(18,574)	(18,574)	(18,574)
	189,567	199,328	200,630
Earnings from continuing operations (excluding reduction to net recoverable cost)	$ 54,803	$ 45,042*	$ 43,740
Increase in specific prices (current cost) of property, plant and equipment held during the year			$ 67,686
Reduction to net recoverable cost		$(103,692)	(18,568)
Effect of increase in general price level			(151,580)
Excess of increase in general price level over increase in specific prices after reduction to net recoverable cost			(102,462)
Gain from decline in purchasing power of net amounts owed		62,665	62,665
Net		$ (41,027)	$ (39,797)

*Including the reduction to net recoverable cost, the earnings (loss) from continuing operations on a constant dollar basis would have been $(58,650) for 1979.

Five Year Comparison of Selected Supplementary Financial Data Adjusted For Effects of Changing Prices

	1975	1976	1977	1978	1979
	Years Ended December 31,				
	(In thousands of average 1979 dollars except per share amounts)				
Operating revenues	$114,657	$126,957	$166,134	$208,378	$244,370
Historical cost information adjusted for general inflation:					
Earnings from continuing operations					$ 45,042
Earnings from continuing operations per common share					$ 2.29
Net assets at year-end at net recoverable cost					$428,877
Current cost information:					
Earnings from continuing operations					$ 43,740
Earnings from continuing operations per common share					$ 2.20
Excess of increase in general price level over increase in specific price after reduction to net recoverable cost					$102,462
Net assets at year-end at net recoverable cost					$428,877
General information:					
Gain from decline in purchasing power of net amounts owed					$ 62,665
Cash dividends declared per common share	$ 1.70	$ 1.81	$ 1.93	$ 1.91	$ 1.88
Market price per common share at year-end	$ 24.36	$ 29.95	$ 25.13	$ 21.31	$ 17.27
Average consumer price index	161.2	170.5	181.5	195.4	217.5

PNM Statement of Principle

Public Service Company of New Mexico believes that each successive generation's quality of life will be progressively more dependent upon the availability and reliability of electric and water service.

Consistent with this belief, we recognize our obligations to:

Our Customers
An adequate and reliable source of electric and water service at the lowest reasonable cost;

Our Shareholders
A reasonable return on, with optimum security of, their investment;

Our Employees
An objective opportunity to progress and grow through productive and meaningful participation; and

Our Future Generations
A legacy of adequate electric and water service provided through free enterprise with environmental and economic compatibility.

To meet these obligations, we affirm a policy of:

Operating our Company in a responsible manner which reflects the highest corporate integrity;

Providing open communications in order to achieve a high level of understanding and acceptance of our purpose and endeavors;

Sharing our technical and administrative skills with all levels of government to assist in assuring the best decisions are made; and

Promoting, supporting and participating in worthwhile community activities and development.

J. D. Geist, President

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J. D. GEIST* — *President, Public Service Company of New Mexico*
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G. A. SCHREIBER* — *Chairman of the Board of Directors, Public Service Company of New Mexico*
R. H. STEPHENS† — *President, Stephens-Irish Agency — Las Vegas, New Mexico*
E. R. WOOD — *President, Santa Fe Motor Company — Santa Fe, New Mexico*

* *Members of the Executive Committee*
† *Members of the Audit Committee*

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T. P. WARNKE — *District Vice President, San Juan*
W. A. BADSGARD — *Western Division Manager*
L. C. EDWARDS — *Bernalillo Division Manager*
E. L. FOGLEMAN — *Las Vegas Division Manager*
R. H. HALLFORD — *Deming Division Manager*
W. M. HICKS, JR. — *Manager, Water Operations, Santa Fe*
J. L. SMITH — *Belen Division Manager*

Executive Offices

414 Silver Avenue SW, Albuquerque, New Mexico

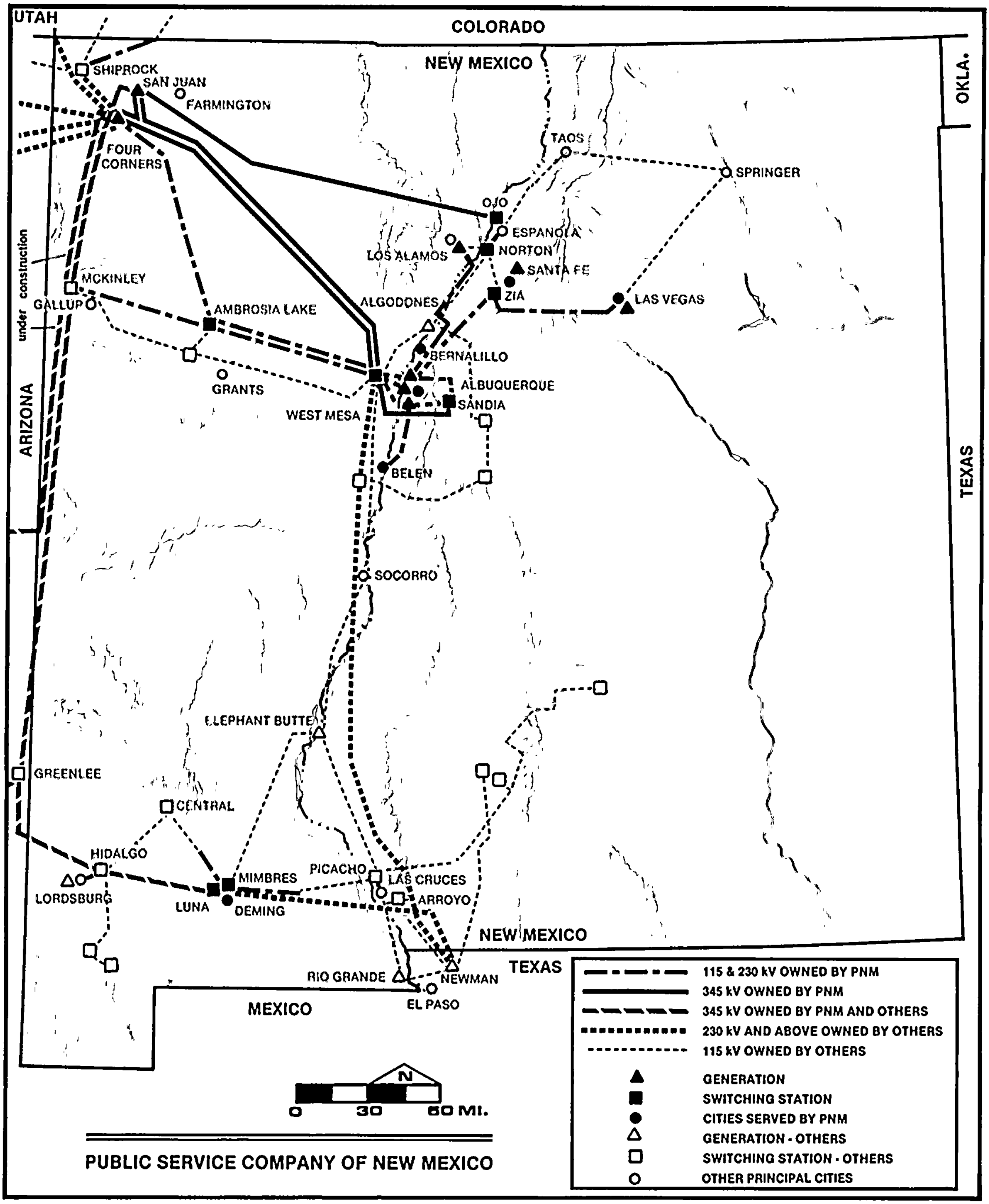
Transfer Agents

Albuquerque National Bank, Albuquerque, New Mexico
Chemical Bank, New York, New York
Irving Trust Company, New York, New York

Registrars

First National Bank in Albuquerque, Albuquerque, New Mexico
Chemical Bank, New York, New York
Irving Trust Company, New York, New York

System Map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TAOS
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115 kV OWNED BY OTHERS
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SWITCHING STATION
CITIES SERVED BY PNM
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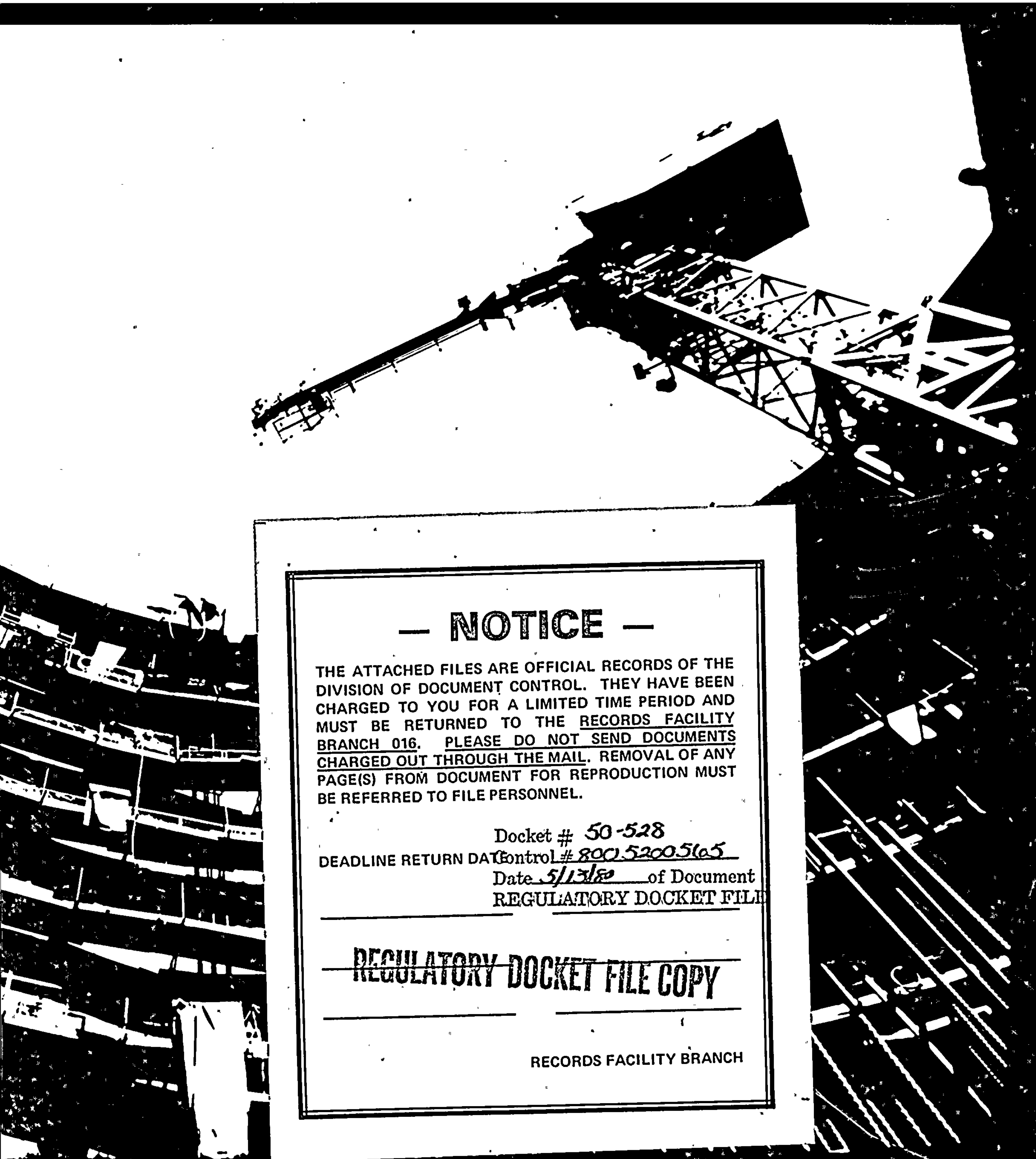
1979 Annual Report
El Paso Electric Company



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Contents

Dividend Reinvestment

Another year of growth was noted in the Company's Dividend Reinvestment and Stock Purchase Plan. The plan is available to holders of record of Common Stock and is a convenient method of investing dividends and optional cash payments in new shares without payment of issuing expenses. An enrollment card may be obtained by writing the Company Secretary.

About the Cover
An on-site look at construction in progress inside the containment building at Palo Verde Nuclear Generating Station Unit No. 2.

Highlights

	At December 31, 1979		1978	
Operating Revenues (000)	$ 159,712		$ 136,556	
Operating Expenses (000)	$ 135,643		$ 116,107	
Net Income (000)	$ 23,190		$ 16,024	
Net Income per share (Common)	$ 1.45		$ 1.30	
Dividends per share (Common)	$ 1.07		$ 1.02	
Book Value per share	$ 10.44		$ 10.01	
Common Shares Outstanding	14,503,373		11,191,371	
Number of Common Shareholders	32,995		25,633	
Number of Customers	175,311		168,009	
Number of Employees	965		908	
Peak Load	688,000	KW	690,000	KW
Net Generating Capacity	982,000	KW	982,000	KW
Average Residential Use	6,072	KWH	6,153	KWH
Fuel Expense (000)	$ 81,669		$ 73,447	
Energy Sales (MWH)	3,424,284		3,320,649	
Electric Plant (000)	$ 561,783		$ 438,085	

The Electric Company

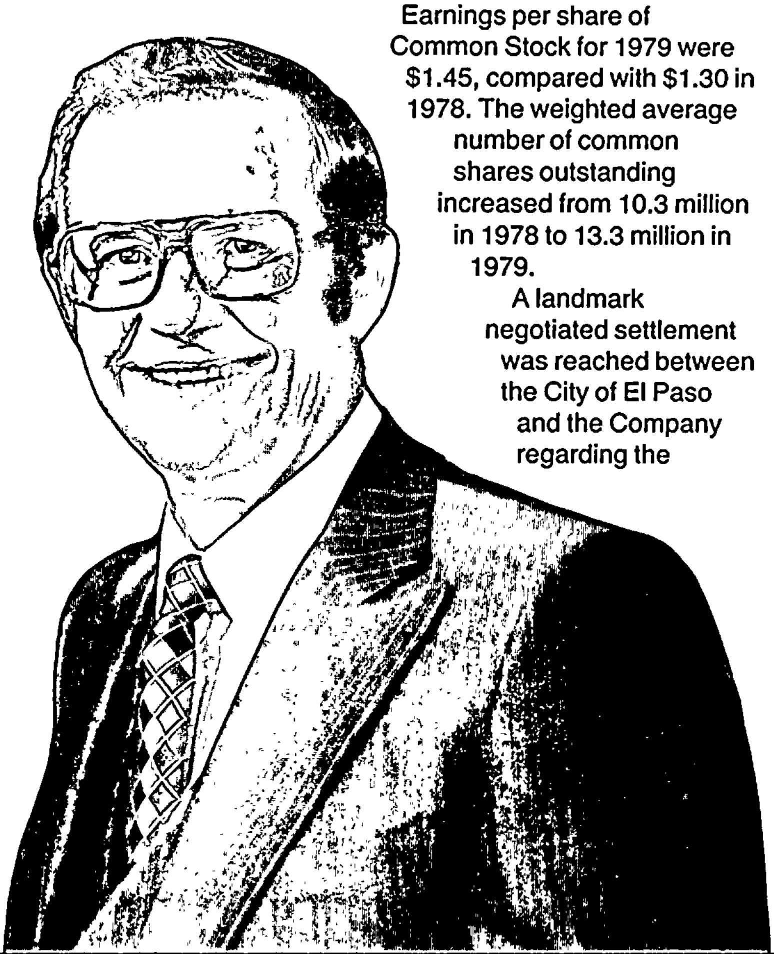
El Paso Electric

The 1970's were a period of vast technological, industrial, economic and social change. The 1980's should also prove to be a pivotal period for the electric utility industry since we will continue to need additional energy facilities in the future despite reduced economic growth projections.

The 1980's will be an era of great challenges as reliance on imported petroleum products continues while we make the difficult and expensive transition from a petroleum-based economy to alternative energy resources. You will find in this report how The Electric Company is adjusting its operations and plans to address the new challenges it faces.

Dividends in 1979 totaled $1.07 a share, up 5¢ from 1978. The quarterly dividend on Common Stock was increased from 25¢ to 27-1/2¢ per share in September, 1979. Dividends on Common Stock continued, without interruption, as they have since distribution of the Common Stock to the public in 1947.

Operating revenues for 1979 reached approximately $160 million. Total operating expenses were approximately $136 million, an increase of 17% over 1978. We continue to exercise careful control over expenses to insure that electricity is generated or purchased at the lowest possible cost to our customers. Fuel costs represented 60% of the Company's total operating expenses.



Earnings per share of Common Stock for 1979 were $1.45, compared with $1.30 in 1978. The weighted average number of common shares outstanding increased from 10.3 million in 1978 to 13.3 million in 1979.

A landmark negotiated settlement was reached between the City of El Paso and the Company regarding the Company's Texas rate increase request filed in June, 1979. Under terms of the settlement the Company received an $11.9 million annual revenue increase for its Texas service area. The negotiated settlement was adopted by the Public Utility Commission of Texas for the unincorporated areas and for the balance of the Company's Texas service area. To my knowledge this was the first time since the implementation of the Texas Public Utility Regulatory Act of 1975 that a municipality and an electric utility reached a negotiated settlement of a major electric rate case. In the settlement the Company was authorized a 15.5% return on common equity and the new rates were made effective with November, 1979 billings, two months earlier than had the case followed the usual course of appeal to the Public Utility Commission of Texas.

In New Mexico the Company applied for a $7 million increase in December, 1978. The New Mexico Public Service Commission authorized an increase of $1.9 million and disallowed the inclusion of construction work in progress (CWIP) in rate base relative to the Palo Verde Nuclear Generating Station. The Company presently has an application pending for an $8.9 million increase in New Mexico including $1.6 million interim rate relief. Testimony has been presented to the commission regarding the interim rate relief and a decision is expected by May 1, 1980.

The funds for the Company's construction program are obtained from internally generated funds and sale of securities and long-term borrowings. Construction spending for 1979 was about $130 million and approximately $158 million is budgeted for 1980.

Achieving adequate rates is a challenge for our Company and the utility industry in general. Such nationwide problems as double-digit inflation, soaring interest rates, higher raw energy prices and increased environmental and other regulatory requirements have required periodic rate increases. Rate structures that accurately reflect our cost to serve each customer and provide a fair return to investors are an integral part of the Company's rate requests.

Since the late 1920's The Electric Company has been largely dependent on natural gas and oil for boiler fuel. In 1969 the Company's cost of fuel was $6.5 million. The Company's total fuel bill in 1979 was approximately $81.7 million, representing an 11.6 times increase over the past ten years, primarily the result of the fuel shortage and rapid inflation. The price of oil and natural gas has increased much faster than the inflation rate and fuel continues to be the Company's largest expense item.

Your Company must contend with diminishing and uncertain petroleum fuel supplies, inflationary costs, major capital requirements, and shifting – often conflicting – government policies and regulations to provide reliable electric service to a growing service territory. Our best hope to lessen the impact of these soaring costs and to lend stability to our customers' rising energy bills is the Palo Verde Nuclear Generating Station. Your Company owns an undivided 15.8% interest in the 3,810 megawatt Palo Verde Project, now under construction 50 miles west of Phoenix, Arizona. Nuclear power will be increasingly relied upon by the Company the remainder of this century to make it less dependent on risky petroleum fuels.

Public awareness of nuclear power was intensified in 1979 as a result of the accident at the Three Mile Island (TMI) nuclear power station in Pennsylvania. The accident at TMI was the most serious in the history of commercial nuclear power and opponents quickly seized the opportunity in an attempt to influence public opinion. At TMI not a single injury or fatality resulted. No energy source is 100% risk-free and the risk to the public posed by operating nuclear plants is less than those posed by other methods of generating the same quantity of electricity. Nuclear power will become an even safer and more efficient energy source as a result of industry and government actions following the TMI incident as explained elsewhere in this report.

Our customers view higher energy prices as particularly upsetting when accompanied by the dramatic rise in other living costs. A number of factors must be addressed during the near term by consumers, business and government to exert downward pressure on inflation. These include the reduction of excessive government spending, elimination of unnecessary and costly government regulations, reduction of business taxes and institution of measures to boost productivity and stimulate investment. The Electric Company intends to continue its efforts to hold the line on costs wherever possible and continue to speak out whenever necessary to identify actions by government and regulators when their policies will result in increased costs.

The Electric Company works agresively to protect natural resources as well as to comply with the many and proliferating laws and regulations in the environmental area. The Company is working on a number of projects to improve the environment primarily at the Four Corners Power Station. Construction improvements are continually being made to insure that all facilities are in satisfactory compliance with environmental requirements.

Looking back over the last decade it can be said that your Company did its job of providing a necessary product exceptionally well in the face of many adversities.

This record of accomplishment is a tribute to the people of The Electric Company working together to serve the customers and communities in our service territory.

The many successes we have experienced over the years have been due to the combined efforts of many individuals: employees, directors, friends, and Shareholders. We look forward to their continuing support and active participation in meeting the challenges of the years ahead.

Evern R. Wall

Evern R. Wall
President and Chief Executive Officer

A Report on The Palo Verde Nuclear Generating Station:

Nuclear power is a proven technology for generating electricity economcally, cleanly and safely and now provides a substantial portion of the electricity consumed in the United States, saving thousands of barrels of oil daily.

At The Electric Company nuclear power will play an increasingly significant role in satisfying the energy demands of our customers beginning in 1983 when the first unit at the Palo Verde Nuclear Generating Station is scheduled to go into commercial operation.

The Electric Company owns a 15.8% undivided interest in the Palo Verde Project, 50 miles west of Phoenix, along with four other Southwestern utilities: Public Service Company of New Mexico, Southern California Edison Co., Arizona Public Service Company and Salt River Project. The three Palo Verde units, each with a capacity of 1,270 megawatts, are scheduled for commercial operation in 1983, 1984, and 1986, respectively. Upon completion the Palo Verde Nuclear Generating Station will be the largest nuclear power station in the United States, delivering three times the amount of electricity as the Hoover Dam. The Electric Company will receive 200 megawatts from each unit.

Construction advanced significantly during 1979 on the Palo Verde Station and at year's end Unit 1 was 57% complete; Unit 2 was 26% complete; and Unit 3 was 6% complete. The Company's estimated share of the cost of the Palo Verde Project, including transmission facilities and Allowance for Funds Used During Construction (AFUDC), is approximately $853.9 million. As of December 31, 1979, the Company had invested approximately $241.3 million in the Project.

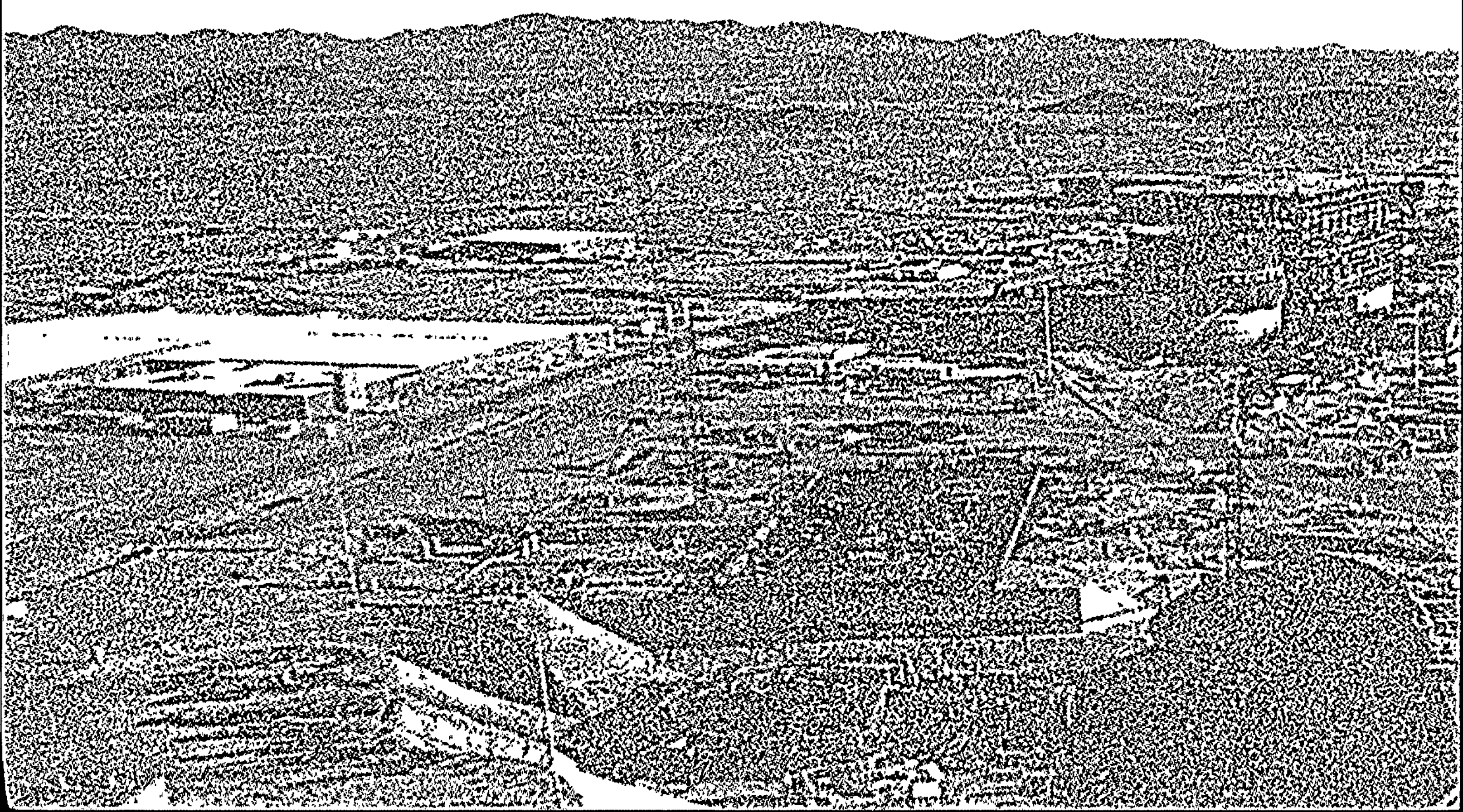
Labor and weather related problems at the site resulted in a one year delay in the completion of Unit One until May of 1983 while the other two units remained on schedule.

When nuclear power becomes a part of the Company's fuel mix in the 1980's, it will begin reducing the Company's dependence on oil and natural gas and help stabilize rising energy costs. The Electric Company is confident its investment in Palo Verde will provide important economic benefits in the future. In 1979 commercial nuclear power saved the nation approximately 425 million barrels of oil while producing about 11.5% of all the electricity produced in this country. At the same time the Organization of Petroleum Exporting Countries (OPEC) raised oil prices by an average of 94% with further increases a certainty.

The nuclear industry experienced its first major industrial accident in the 25-year history of commercial nuclear power generation in 1979 at the Three Mile Island power station in Pennsylvania. The public was made more acutely aware of the nuclear industry as a result. While the planned nuclear safeguards functioned at TMI and the public was protected, several lessons were learned from the incident which will result in an even safer nuclear industry.

Immediately after the TMI incident the Palo Verde participants organized a task force composed of experts from among the participants and suppliers of major components to conduct a thorough and exhaustive review of the safety related systems at Palo Verde. The task force is expected to issue its final report in mid-1980.

The industry demonstrated its seriousness and dedication to nuclear safety planning and operation in the immediate aftermath of the TMI incident, anticipating the "fundamental changes" recommended by the President's



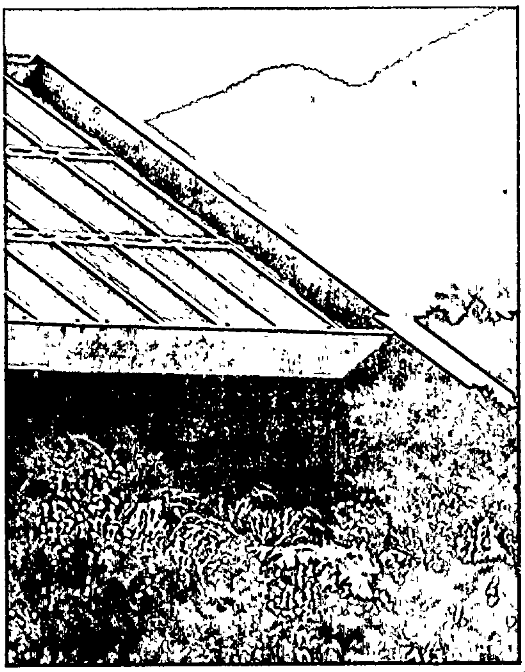
Commission on the Accident at Three Mile Island. The industry moved swiftly to establish the Nuclear Safety Analysis Center (NSAC) through the Electric Power Research Institute and the Institute of Nuclear Power Operations (INPO) which will set standards of excellence for operation and management of nuclear power programs. Another major component of the industry's efforts is a mutual insurance company to help protect utilities against some of the financial consequences of a prolonged nuclear reactor outage. Improved reactor operator training, equipment and controls improvement, and improved operating procedures are also being addressed.

The Electric Company views the future of nuclear power with confidence as the world petroleum situation tightens and international politics continues to distort the oil markets.

The energy shortage, clearly signaled at least in the late 1960's and confirmed by the arab oil embargo of 1973-74, is not difficult to comprehend. The world, and the United States in particular, simply has been consuming and continues to consume energy at a rate faster than new energy sources are being developed. Since before 1956 our nation has been using more energy than it produced domestically and since 1972 that gap has widened dramatically. OPEC has pushed the price of their exports higher since 1974 while in the United States federal controls on oil and natural gas pricing have discouraged production and stimulated use by maintaining prices at artificially low levels.

The Electric Company is examining various energy sources for the long term and contemplates additional use of nuclear and coal in the foreseeable future. The Company participates in a variety of Research and Development programs through the Electric Power Research Institute and is increasing its level of participation with The Department of Energy, private research organizations and area universities including several local solar, geothermal and wind energy projects. Nuclear fusion will prove to be a valuable energy option and El Paso Electric is backing fusion research through the Texas Atomic Energy Research Foundation.

All research is vital to the future application of alternate energy resources and it is part of the commitment The Electric Company has made to its customers as a major energy supplier. Management remains convinced, after considering all the immediately available options, that nuclear power is the safest, most economical and environmentally superior method of generating electricity particularly in the 1980's and 1990's.



Solar collectors – Las Cruces, N.M.

Palo Verde Nuclear Generating Station

Throughout the 1970's El Paso and surrounding areas experienced substantial growth and development and has continued to develop as a major regional economic, trade and population center of the Sun Belt.

The El Paso area economy exhibited unusual strength in the 1970's and its solid development was supported by a modern and broad-based economy. One of the most solid indicators is employment which increased 15.6% during the past five years.

During the 1970's, the population of El Paso increased 27% to 410,000 and is projected to increase an additional 40% during the 1980's.

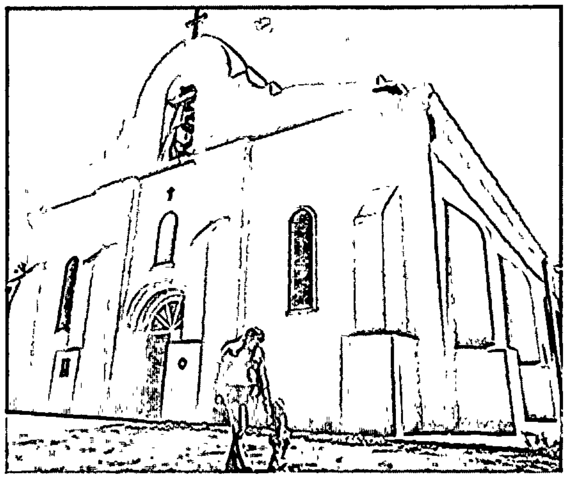
The economic impact of new industries locating in El Paso in 1979 is approximately $1.1 billion as calculated by the Texas Industrial Commission. By the end of 1979 a total of 27 new industrial locations in El Paso and vicinity had been announced. This growth will provide about 3,000 new jobs. Interest in El Paso and twin plant locations in Ciudad Juarez, Mexico remains high and several large foreign and domestic firms have indicated an interest in far West Texas.

More than 105 American companies are operating under the Mexican Border Industrialization Program, or twin-plant concept. When Juarez begins to receive natural gas through a pipeline now under construction from the Mexican interior, the twin-plant operation could expand significantly, resulting in a strong economic impact on the entire area. In addition, El Paso is now the busiest international port of entry in the United States as measured by border crossings between the United States and Mexico.

Construction activity in 1979 continued at a moderate pace in El Paso and Las Cruces, New Mexico, the largest community served by the Company in its New Mexico jurisdiction. The value of all building permits in El Paso totaled approximately $238 million in 1979, a nine percent increase over 1978. Approximately $20 million of the 1979 total is for the new 18-story El Paso Natural Gas Company building now under construction in downtown El Paso.

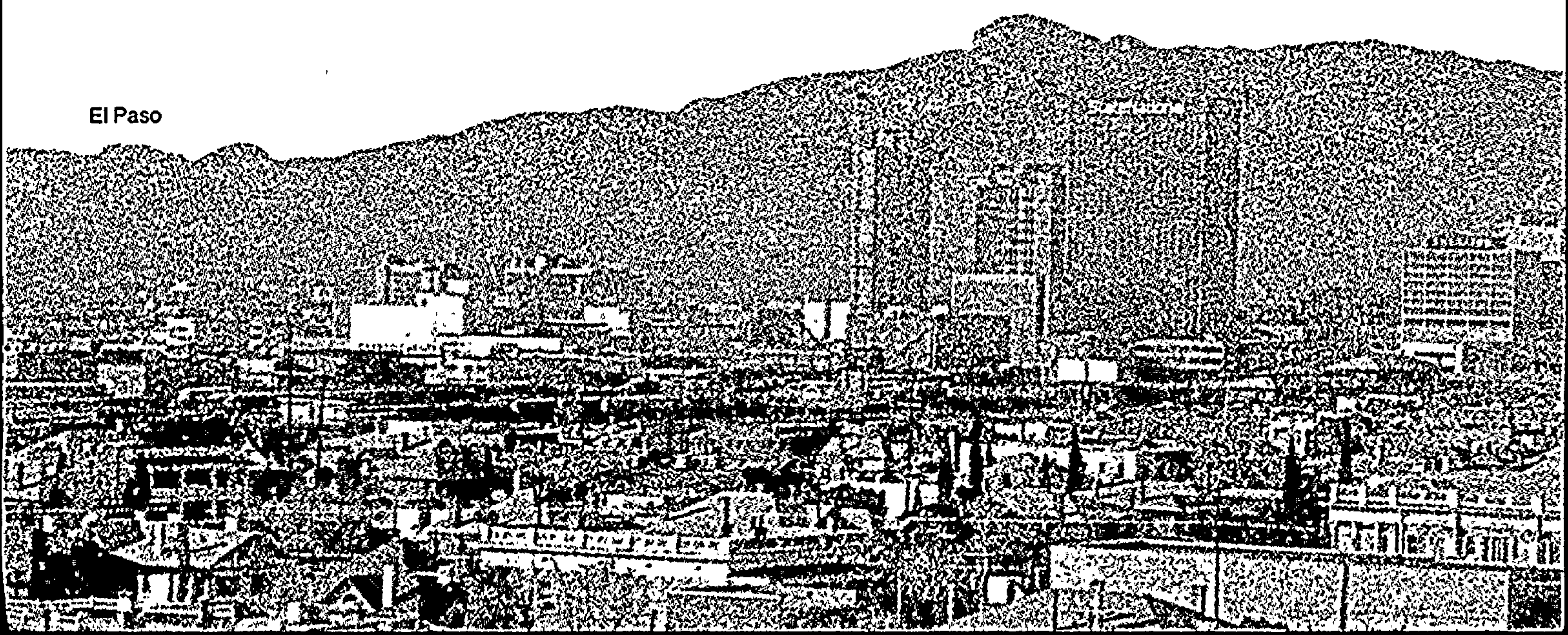
A decrease in construction of single family units from 3,153 in 1978 to 2,606 in 1979 appears to be the result of sharply higher interest rates during the year.

Retail sales in El Paso have established new highs almost every year. In 1979 retail sales were up about 15 percent over 1978. Military installations continue to be major economic factors in the Company's service area. Fort Bliss Army Air Defense Center, William Beaumont Army Medical Center, White Sands Missile Range and Holloman Air Force Base are major facilities served by the Company.

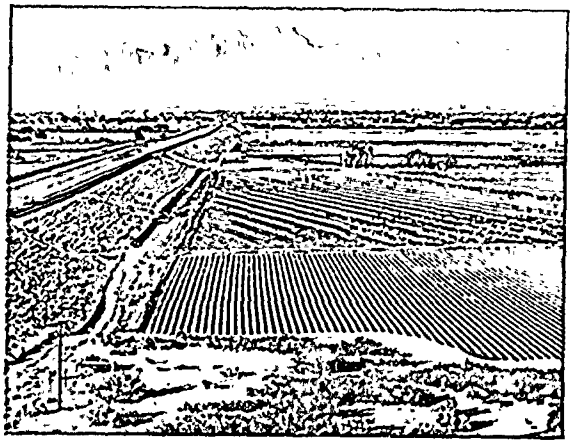


Ysleta Mission

El Paso



Las Cruces



The Company's Mesilla Valley Division, headquartered in Las Cruces, New Mexico, also continued to attract new residents and businesses in 1979. Building permit totals for 1979 in Las Cruces declined somewhat from last year's record pace. The total for 1979 was $29.3 million compared with $38.3 million in 1978. Las Cruces was designated a Standard Metropolitan Statistical Area in 1979 as a result of a special census. The population of Las Cruces grew from 48,000 in 1978 to 50,000 in 1979. At the end of the year the Company was serving 34,292 customers in New Mexico, five percent more than in 1978. Business relocations to Las Cruces include the Joy Canning Company, Furtex, Inc., a synthetic fur manufacturer, and Davidson Rubber Company, an auto parts manufacturer.

In 1979, The Electric Company added approximately 7,300 new customers to its system reflecting the steady growth of the Southwest as an attractive place to live and work.

Total system sales climbed to 3,424,284 megawatt-hours (MWH), a 3.1 percent increase over 1978.

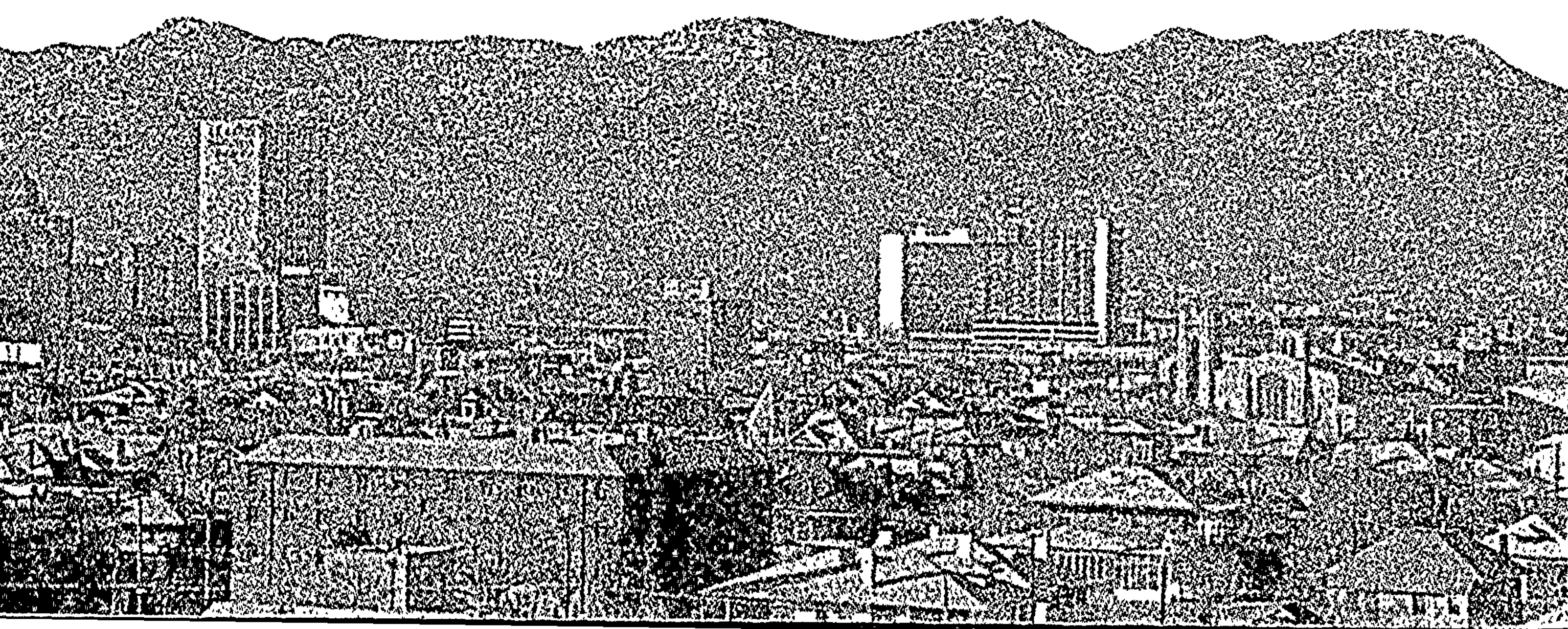
The commercial and industrial customer category, including schools, hospitals and other public facilities, as well as stores and offices, accounted for 1,632,000 MWH, up four percent from 1978. Residential customers accounted for 938,000 MWH, up three percent from 1978. The average residential customer used 6,072 KWH, a one percent decrease in 1979. The average cost per KWH for residential customers was 5.6¢.

The annual growth rate in energy sales has slowed during the 1970's. Conservation and increased energy price awareness, while expected to continue, should not totally negate the impact of customer growth.

The 1979 maximum one hour peak demand on the system of 688,000 KW occurred on July 10 and was slightly less than the all-time high system peak of 690,000 KW established in 1978.

The El Paso Electric 1979 net system capacity was 982 megawatts, composed of 498 megawatts at Newman Power Station in El Paso; 372 megawatts at the Rio Grande Power Station, five miles from downtown El Paso in New Mexico, and a seven percent entitlement, or 112 megawatts, from the coal-fueled Four Corners Power Station near Farmington, New Mexico.

The Company is constructing a 73 megawatt combustion turbine generating station in El Paso to be used for peaking purposes. The unit, capable of operating on oil or gas, is scheduled for operation in the second quarter of 1980. The total estimated cost of the peaking unit is $11 million.



Fuel

The Company's fuel mix in the 1980's will not be derived totally from oil and natural gas as has been the case for much of its 78-year history. The events of the 1970's have served as additional stimulus for recognizing the need to reduce dependence on uncertain and increasingly expensive supplies of oil and natural gas.

Natural gas in 1979 provided 79% of the Company's fuel mix. The remainder of its fuel requirements were 13% coal and 8% oil. The gas and oil outlook has changed over the decade of the 1970's with even more uncertainty foreseen in the 1980's. The industry continues to receive mixed signals from the government concerning natural gas.

During the past 10 years the Company's total fuel bill increased more than eleven times. Individually, since 1970 the cost of oil has increased approximately 600%, natural gas increased 500% and coal increased 100%. Fuel costs increased approximately $8.3 million in 1979 over 1978 to approximately $81.7 million, or approximately 60% of 1979 operating expenses.

The nation's energy policies are designed to reduce dependence on expensive depleting petroleum fuels and to encourage conversion to more abundant alternative fuel supplies such as coal and nuclear power. The National Energy Act goes so far as to prohibit new electric power plants from using natural gas or petroleum as a primary energy source except in certain cases and also requires the phasing out of these fuels in existing plants.

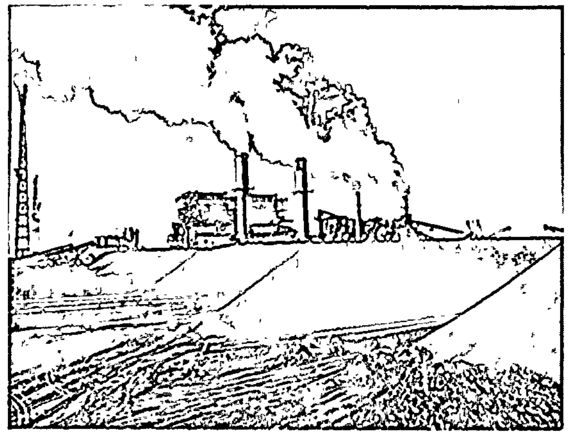
Converting to alternative fuel sources requires an extensive financial commitment by the Company but it is a commitment the Company must undertake in order to provide adequate and reliable electric service in the future at the most economical price.

The Palo Verde Nuclear Generating Station represents the Company's effort to reduce substantially the use of oil and gas and provide electricty to a growing service area at the most reasonable cost possible. With the Palo Verde Station the Company will regain some control over fuel costs by using uranium, one of the only viable domestic fuels available. The participants in the Palo Verde Project have firm contracts for the supply of uranium concentrate to fuel the three units extending to the year 2003. In addition, the participants have acquired a 50% interest in and are developing 60,000 acres of uranium properties in Wyoming which will further assure Palo Verde fuel requirements.

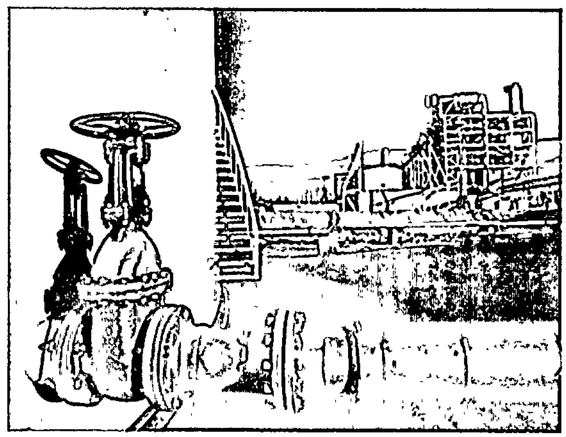
The Company began diversifying its fuel mix in the late 1960's when it became a part owner of the coal-fueled Four Corners Power Station. By the 1990's electric generation is expected to be approximately 60% coal and nuclear-fueled.

Franklin Land and Resources, Inc. is the Electric Company's wholly owned subsidiary, organized to secure property and water rights for the Company's various projects and business-related needs, primarily plant sites and water for cooling purposes at generating plants.

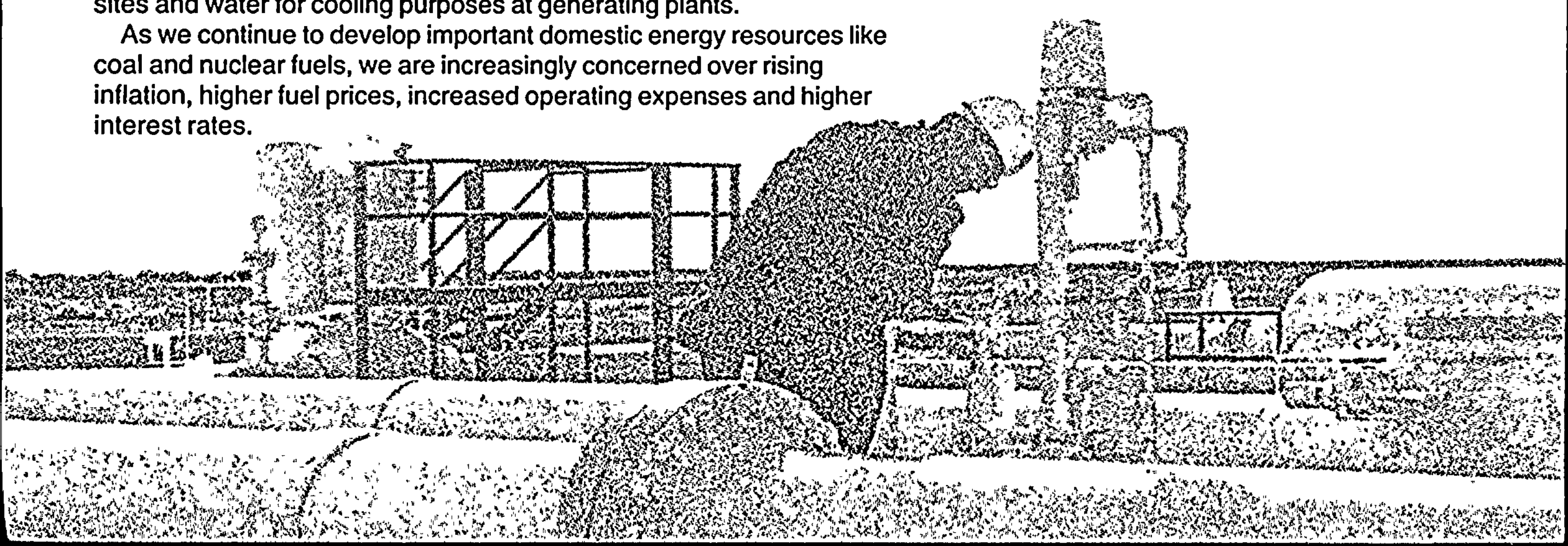
As we continue to develop important domestic energy resources like coal and nuclear fuels, we are increasingly concerned over rising inflation, higher fuel prices, increased operating expenses and higher interest rates.



Four Corners Power Station



Oil Storage Tank
Rio Grande Power Station



Rates and Regulation

Converting to alternate fuel sources to assure an adequate supply of electricity for the coming decades has required an extensive financial commitment by The Electric Company. It has been necessary for the Company to seek rate increases during the last few years to support its construction program and to offset the effects of persistent high inflation.

In 1979, the Company and the City of El Paso reached a landmark negotiated rate settlement calling for a revenue increase of $11.9 million, a 15.5% return on common equity and an effective date two months earlier than would have otherwise been possible. In addition, the negotiated settlement eliminated the prospect of an appeal to the Public Utility Commission of Texas, which has been costly in the past and provides an opportunity for the City and the Company to undertake settlements of pending litigation without further appeals. If no further appeal to past cases is made by the City, the time and money which would otherwise be spent solving these problems in court will be saved.

The negotiated rate settlement with the City of El Paso was the first since the implementation of the Texas Public Utility Regulatory Act of 1975. The Act created the Public Utility Commission of Texas as the appellate jurisdiction over electric rates and services in Texas municipalities and empowered it with original jurisdiction in unincorporated areas of the state. The PUC and other incorporated areas later adopted the City settlement to cover the balance of the Company's Texas service territory. Cooperation between the City and The Electric Company is very important to the community, and this agreement should pave the way to improved relations and cooperation for the benefit of all concerned since continued community support is essential if long-range energy needs are to be satisfied.

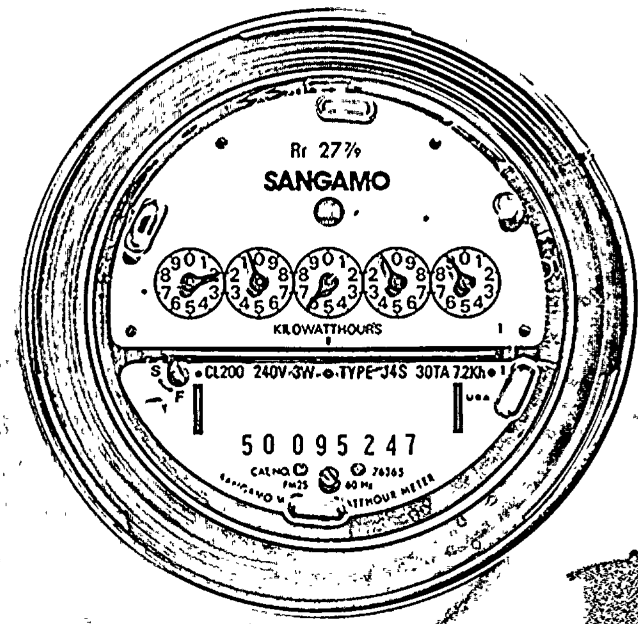
We believe it is clearly advantageous from an economic and financial standpoint to negotiate an agreement of this nature rather than undergo lengthy formal litigation over many months or even years at great expense to the Company and its customers.

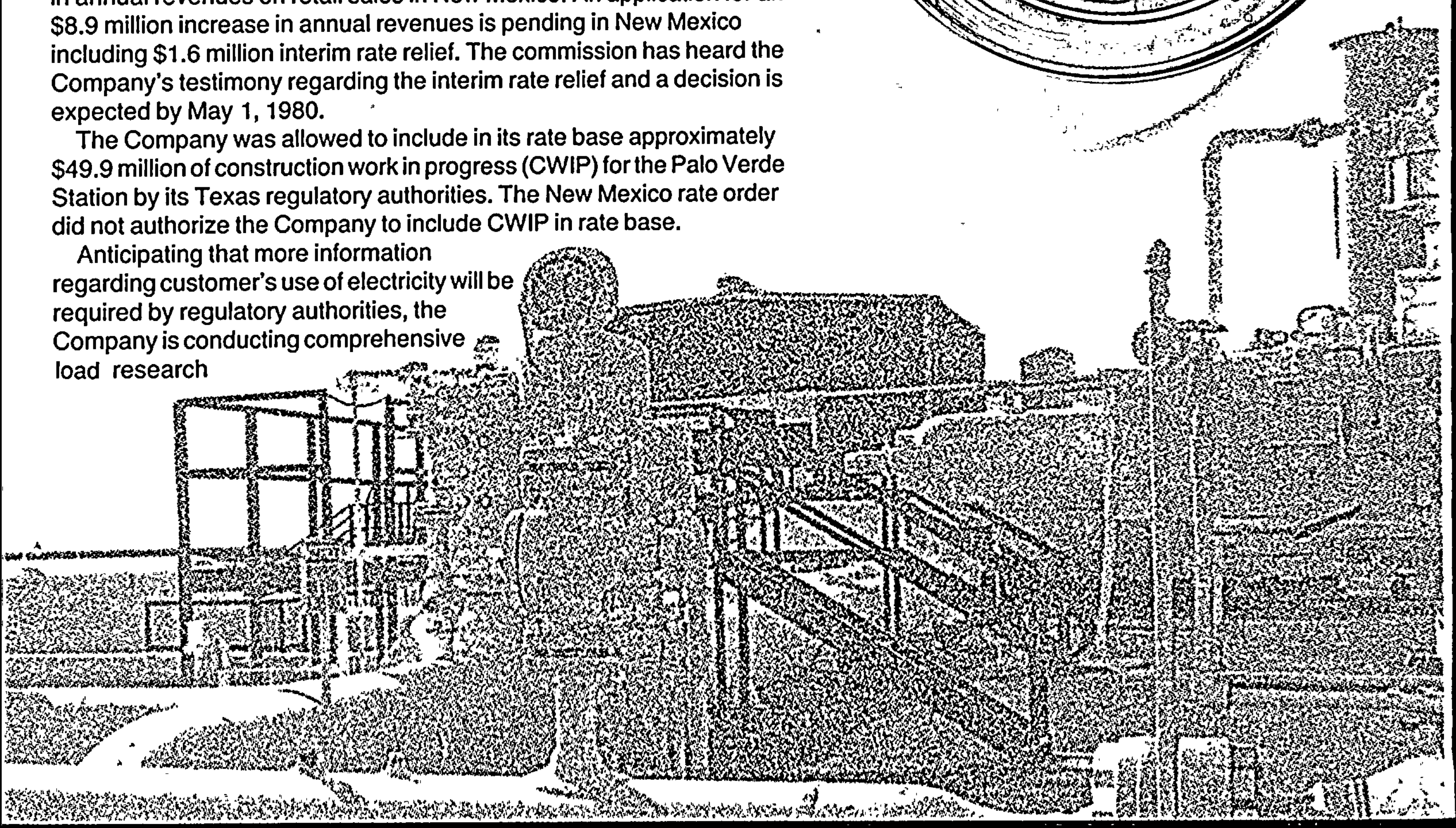
The Company has appealed the New Mexico Public Service Commission decision that granted the Company a $1.9 million increase in annual revenues on retail sales in New Mexico. An application for an $8.9 million increase in annual revenues is pending in New Mexico including $1.6 million interim rate relief. The commission has heard the Company's testimony regarding the interim rate relief and a decision is expected by May 1, 1980.

The Company was allowed to include in its rate base approximately $49.9 million of construction work in progress (CWIP) for the Palo Verde Station by its Texas regulatory authorities. The New Mexico rate order did not authorize the Company to include CWIP in rate base.

Anticipating that more information regarding customer's use of electricity will be required by regulatory authorities, the Company is conducting comprehensive load research studies. This information will be utilized for engineering and system planning as well as for regulatory requirements.

The Company continually strives to maintain rates which adequately cover all costs of service, including fair compensation to investors, and which preserve its financial integrity and ability to attract the capital required to build the facilities to meet the needs of all customers. As the economic and regulatory factors described throughout this report continue to affect the Company's financial results and because the rates approved have been lower than requested, it will be necessary for the Company to file for additional rate relief in the near future.





In a world where government actions and public opinion may have as much impact on business decisions as market considerations, the responsibilities of management must extend beyond day to day operations. Responding to the impact of these external forces on the business environment The Electric Company, like other electric utilities, has started speaking out and providing information to its customers on important issues.

Throughout the 1970's energy conservation and proper energy management have been the predominant theme of corporate communications. This has been broadened to include pertinent information on such matters as the Company's construction program, electrical safety and nuclear power.

The Three Mile Island accident created some confusion and uncertainty regarding nuclear power in the United States. To provide accurate information and to facilitate better public understanding of nuclear power in general and the Company's participation in the Palo Verde Nuclear Generating Station, a thorough mass-media campaign addressing these issues was launched in 1979. Former astronaut Scott Carpenter appears in many of the advertisements speaking on behalf of The Electric Company and Palo Verde.

These messages have been well-received and are carrying the Company's message to customers: That Palo Verde and nuclear energy are essential to the continued economic well-being in the area served by the Company and that despite setbacks in 1979 nuclear power is as safe as any technology ever developed by man and safer than most comparable industrial undertakings.

The Company recognizes the diverse cultural backgrounds which exist throughout its service area and has attempted to tailor its communications to meet the needs of this population. Most corporate communications with customers are produced in both English and Spanish.

The public demand for the Company's various printed materials regarding electrical safety, energy conservation, and alternative energy sources has been very strong with thousands of copies distributed to the public, local schools and organizations during the year. The Company's standardized monthly bill insert "The Electric Guide" has been favorably received by customers.

Much of this material is utilized by the Company's Community Services Section's public school energy education program.

Programs on the environment, solar energy, conservation, nuclear energy, safety and field trips to Company facilities are provided to consumers and area school districts. In addition, the Company has provided much valuable information to several schools through the Edison Electric Institute High School Grant Program.

The Company's Energy Utilization and Conservation Section is trained and staffed to provide energy management information and energy audits for residential and commercial customers. The National Energy Act requirements for utilities to offer home energy audits starting in 1980 will pose no unusual problems for the Company since this activity has been offered for a number of years.

The Company continues to encourage construction of the WISE (Weatherized and Insulated to Save Energy) Home among local home builders as well as retrofitting existing homes to energy efficient standards.

Employees

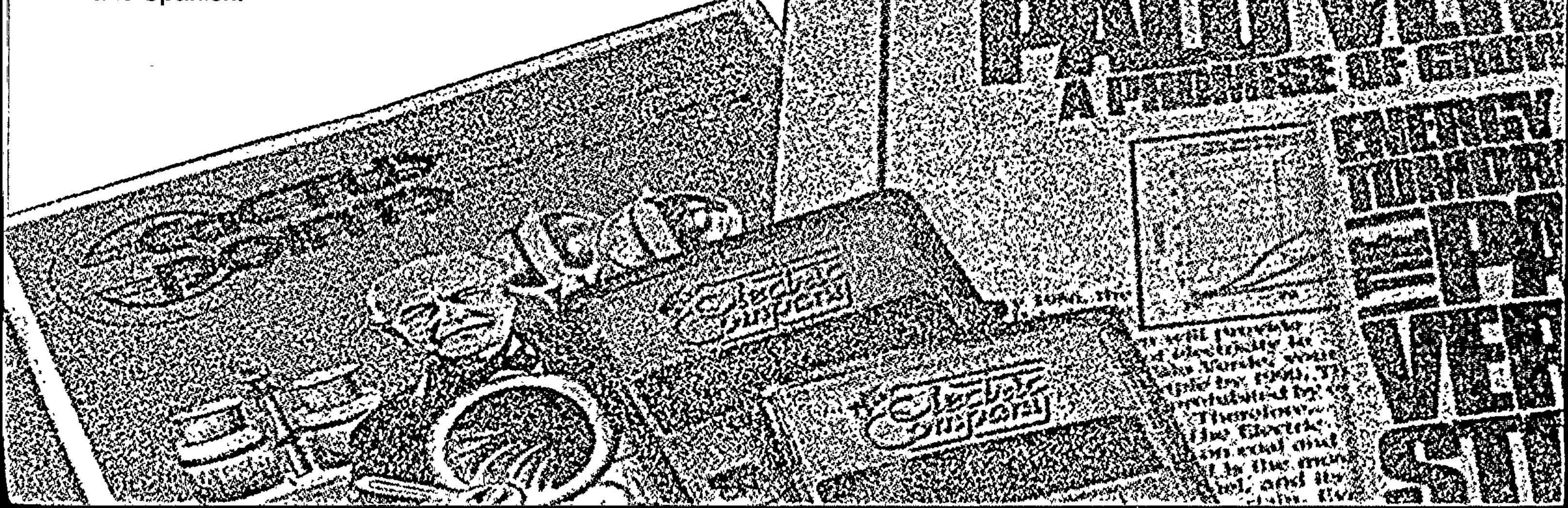
The Company's success in accomplishing its stated goals of:

- protecting and enhancing the investment of its shareholders;
- providing an enriching and satisfying place to work;
- providing the best possible service to its customers at a reasonable cost;

can be attributed to the skills and contributions of its dedicated employees.

At year-end 1979 the Company had 965 employees in its two-state service area.

Employees continued to demonstrate interest in the Company's Employee Stock Purchase Plan through payroll deductions to purchase common stock. Approximately 180 of the Company's employees were participating at the end of the year. The Company also offers an Employee Stock Ownership Plan (ESOP) which provides employees with greater participation in the ownership of the Company under attractive terms and provides the Company with additional tax credits towards its federal income tax liability.



- The Company continues to emphasize training in all its operations to further upgrade the quality of service as well as employee performance and productivity.

A two-year labor agreement between the Company and Local 960 of the International Brotherhood of Electrical Workers, which represents 340 bargaining unit employees, was finalized in February, 1980. The contract became effective March 1, 1980, and contains a mutually acceptable wage and benefit package for the IBEW.

The Company's move to its new headquarters in the historic Mills Building in downtown El Paso was completed in the summer of 1979. The renovated Mills Building provides expanded and economical facilities conducive to the orderly and efficient operations of a growing employee family.

The first woman director of El Paso Electric Company was elected during the annual meeting of shareholders in May as one of two new directors. Mrs. Josefina A. Salas-Porras is executive director of BI Language Services, a firm she founded in 1970, and also serves as a director of the El Paso branch of the Federal Reserve Bank of Dallas.

Leonard A. Goodman, Jr., general agent for John Hancock Mutual Life Insurance Company, was also elected to the Board. Mrs. Salas-Porras and Mr. Goodman succeeded former Company president, Chairman of the Board and retiring director Dennis H. Lane and retiring director Dr. Joseph R. Smiley. Dr. Smiley and Mr. Lane served as advisory directors to the Board during 1979.

Financing

During 1979 the Company's construction program, beyond internally generated cash, was funded by the sale of a combination of Common Stock, Preferred Stock, First Mortgage Bonds, and various banking arrangements. The permanent financing provided aggregate gross proceeds to the Company of approximately $107.8 million.

To finance the Company's construction program in the 1980's it is estimated that funds generated from operations will provide approximately 30% to 32% of the cash required. Additional financing will come from sources outside the Company and will be influenced by market conditions, earnings performance and reasonable regulatory treatment.

Shareholders authorized additional future financing by approving an amendment to the Restated Articles of Incorporation to increase the number of authorized shares of Common Stock from 15 million to 30 million shares at the annual meeting in May, 1979.

An additional positive long-range financial step was taken in January, 1979, when the Company entered into a nuclear fuel financing arrangement whereby a Trust acquired a portion of the nuclear fuel necessary for the Palo Verde Nuclear Generating Station. Under this arrangement the Company was reimbursed for all previous nuclear fuel expenditures and intends to enter into a basic heat supply contract whereby title to the fuel will remain with the Trust and the Company will make lease payments for the heat generated.

Board of Directors

From left to right – seated

George G. Matkin*
Chairman of the Board, The State National Bank of El Paso; Chairman of the Board PanNational Group, Inc. (13)

Paul Harvey*
Honorary Chairman of the Board of the Company; Honorary Vice President, El Paso National Bank; Chairman of the Board, First State Bank (39)

Evern R. Wall*
President and Chief Executive Officer of the Company (5)

Robert E. Boney*
Investments, Las Cruces, New Mexico (32)

Robert H. Cutler*
Chairman of the Board, Illinois-California Express, Inc.; Chairman of the Board, ICX, Inc. (9)

From left to right – standing

Leonard A. Goodman, Jr.
Chartered Life Underwriter; General Agent, John Hancock Mutual Life Insurance Co. (1)

Tad R. Smith
Attorney; Partner, Kemp, Smith, White, Duncan and Hammond; Counsel for the Company (19)

Josefina A. Salas-Porras
Executive Director, BI Language Services (1)

Ben L. Ivey
Farmer; Director, Chairman of the Board, Bank of Ysleta (10)

*Members of the Executive Committee

( ) Years of Service on the Board

Officers

EVERN R. WALL,
President and Chief Executive Officer
ROLLAND E. YORK,
Senior Vice President
BILLYE E. BOSTIC,
Senior Vice President

HARRY I .ZIMMER,
Vice President
JAMES H. JONES,
Vice President
DONALD G. ISBELL,
Vice President

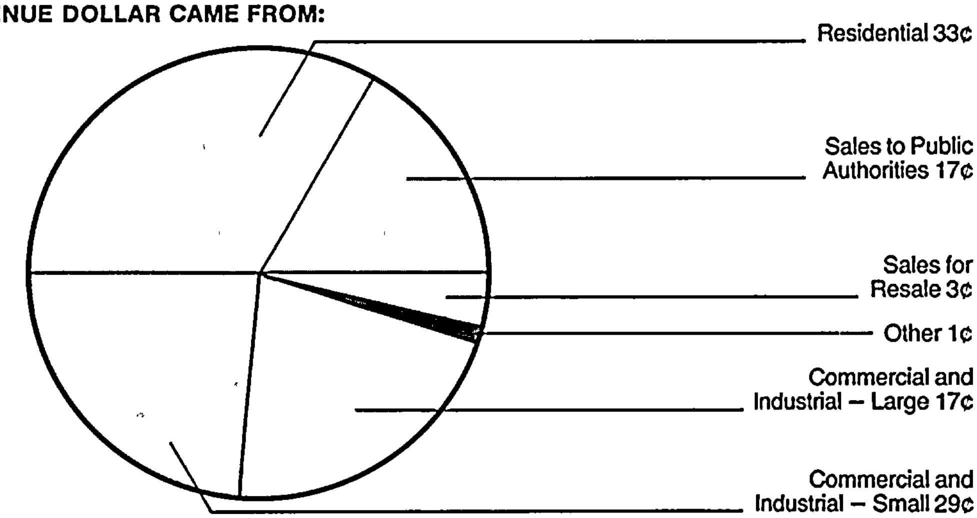
CHARLES MAIS,
Vice President
RALPH G. CROCKER,
Treasurer
WILLIAM J. JOHNSON,
Controller

THETA S. FIELDS,
Secretary
ROBERT L. CORBIN,
Assistant Treasurer and Assistant Secretary

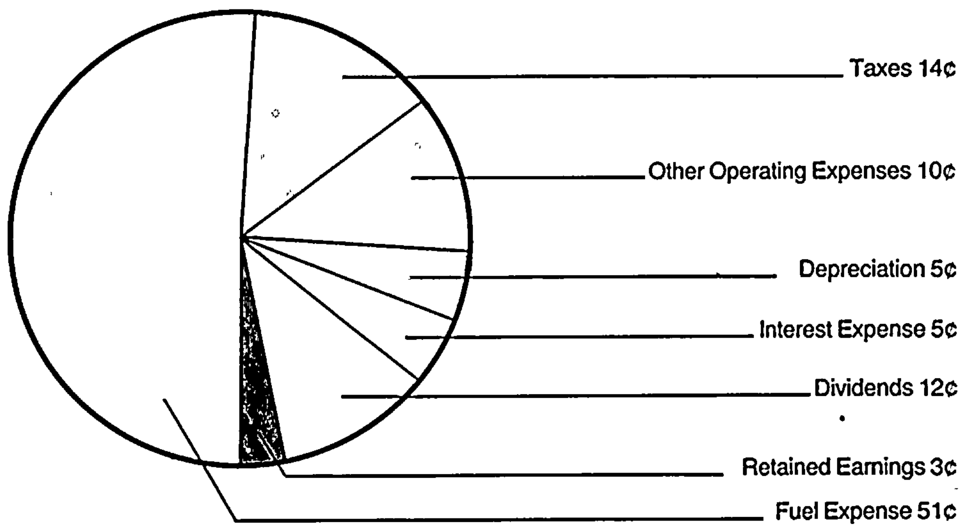
RICHARD E. FARLOW,
Assistant Treasurer
CECELIA R. SHEA
Assistant Secretary

FINANCIAL INFORMATION
(Not covered by Report of Independent Certified Public Accountant)

WHERE THE REVENUE DOLLAR CAME FROM:



WHERE THE REVENUE DOLLAR WENT:



MARKET PRICES OF COMMON STOCK AND DIVIDENDS
(Not covered by Report of Independent Certified Public Accountants)

The following table indicates the high and low bid price of the common stock and dividends paid for the quarters indicated:

Quarter	Bid Price Range		Dividends
	High	Low	
1979			
First Quarter	10⅞	10⅜	$0.26
Second Quarter	10⅝	9⅞	0.26
Third Quarter	11	10	0.275
Fourth Quarter	10⅛	9⅛	0.275
1978			
First Quarter	11⅞	10⅞	$0.25
Second Quarter	11⅜	10⅜	0.25
Third Quarter	11½	10½	0.26
Fourth Quarter	10¾	9⅞	0.26

El Paso Electric Company Common Stock is traded in the over-the-counter market.

The tabulation, which sets forth the high and low bid prices and represents prices between dealers, does not include retail markups, markdowns or commissions.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
CONSOLIDATED BALANCE SHEET
ASSETS

	December 31, 1979	1978
	(In thousands)	
Utility plant:		
Electric plant (Notes B and E)	$561,783	$438,085
Accumulated provision for depreciation	(76,053)	(68,672)
	485,730	369,413
Nonutility property, at cost	2,357	1,563
Accumulated provision for depreciation	(81)	(27)
	2,276	1,536
Current assets:		
Cash (Note F)	10,684	6,032
Accounts receivable (less allowance for doubtful accounts of $205,000 and $228,000, respectively)	18,327	15,325
Federal income taxes refundable	2,694	6,038
Materials and supplies	3,880	2,821
Fuel (Note H)	8,060	8,849
Prepayments	1,712	1,788
Deferred fuel costs	309	1,823
Other	721	303
	46,387	42,979
Deferred charges and other assets:		
Unamortized debt expense	844	808
Other	1,881	1,239
	2,725	2,047
	$537,118	$415,975

The accompanying notes are an integral part of the consolidated financial statements.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY

CONSOLIDATED BALANCE SHEET – (Continued)

LIABILITIES AND SHAREHOLDERS' EQUITY

	December 31, 1979	1978
	(In thousands)	
Capitalization:		
Common stock, no par value, 30,000,000 and 15,000,000 shares authorized, 14,503,373 and 11,191,371 shares issued and outstanding at December 31, 1979 and 1978, respectively (Note C)	$106,329	$ 71,269
Unamortized capital stock expense	(1,029)	(788)
Retained earnings (Note E)	46,126	41,541
Common stock equity	151,426	112,022
Preferred stock – Redemption required, cumulative, no par value, 500,000 and 240,000 shares outstanding at December 31, 1979 and 1978, respectively (Note D)	50,000	24,000
Preferred stock – Redemption not required, cumulative, no par value, 190,000 shares outstanding at December 31, 1979 and 1978 (Note D)	18,873	18,873
Long-term debt (Note E)	171,721	126,152
Total capitalization	392,020	281,047
Current liabilities:		
Current portion of long-term debt (Note E)	4,549	1,045
Notes payable to banks (Note F)	2,125	26,600
Notes payable to other (Note F)	15,290	—
Commercial paper (Note F)	34,332	32,175
Turbine contract payable (Note B)	7,754	—
Fuel purchase commitment (Note H)	7,958	8,747
Accounts payable, principally trade	10,607	8,982
Customer deposits	2,849	2,447
Taxes accrued	6,123	5,419
Deferred income taxes	284	1,021
Interest accrued	3,183	2,831
Other	1,841	955
	96,895	90,222
Deferred credits and other liabilities:		
Accumulated deferred federal income taxes	24,873	17,998
Accumulated deferred investment tax credit	22,537	19,191
Customer advances for construction and other	793	354
	48,203	37,543
Long-term purchase commitment (Note B)	—	7,163
Commitments and contingencies (Notes H and J)		
	$537,118	$415,975

The accompanying notes are an integral part of the consolidated financial statements.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF INCOME

For the years ended December 31, 1979 and 1978

	1979	1978
	(In thousands)	
Operating revenues	$159,712	$136,556
Operating expenses (Notes J and K):		
Fuel	81,669	73,447
Purchased and interchanged power	(3,531)	(2,110)
Operation	20,962	17,722
Maintenance	6,725	5,559
Depreciation (Note B)	8,245	7,361
Taxes (Note G):		
Federal income, current	1,238	(2,617)
Federal income, deferred	6,138	(1,500)
Charge equivalent to investment tax credit, net of amortization	4,083	9,014
Other	10,114	9,231
	135,643	116,107
Operating income	24,069	20,449
Other income:		
Allowance for other funds used during construction (Note I)	7,450	3,197
Other income, net of other expenses	561	954
Federal income taxes (Note G)	(269)	(463)
	7,742	3,688
Income before interest charges	31,811	24,137
Interest charges:		
Interest on long-term debt	11,589	9,477
Other interest (Note B)	7,420	4,041
Other interest capitalized (Note B)	(1,643)	(1,098)
Allowance for borrowed funds used during construction (Note I)	(8,745)	(4,307)
	8,621	8,113
Net income (Note I)	23,190	16,024
Preferred dividend requirements (Note D)	3,948	2,575
Net income applicable to common stock (Note C)	$ 19,242	$ 13,449
Net income per share of common stock (Notes C and I)	$1.45	$1.30
Weighted average number of common shares outstanding	13,252,102	10,333,109

The accompanying notes are an integral part of the consolidated financial statements.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

For the years ended December 31, 1979 and 1978

	1979	1978
	(In thousands)	
Retained earnings at beginning of year	$41,541	$39,056
Net income	23,190	16,024
Amortization of capital stock expense	(134)	(139)
	64,597	54,941
Cash dividends:		
Preferred stock	3,948	2,575
Common stock	14,523	10,825
	18,471	13,400
Retained earnings at end of year	$46,126	$41,541

The accompanying notes are an integral part of the consolidated financial statements.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the years ended December 31, 1979 and 1978

	1979	1978
	(In thousands)	
Source of funds:		
From operations:		
Net income	$ 23,190	$ 16,024
Items not requiring outlay of working capital in the current period:		
Depreciation	8,245	7,361
Deferred federal income tax	6,875	1,354
Investment tax credit	4,083	9,014
Allowance for other funds used during construction	(7,450)	(3,197)
Other	278	223
Funds provided by operations	35,221	30,779
Other sources:		
Sale of nuclear fuel to trust	4,712	—
Sale of preferred stock	26,000	14,000
Sale of common stock	35,060	30,205
Sale of first mortgage bonds	25,000	9,000
Sale of unsecured floating rate promissory note	25,000	—
Long-term mortgages	—	2,124
Long-term purchase commitment	591	563
Advances for construction and other	439	(51)
	152,023	86,620
Application of funds:		
Gross additions to plant	130,282	100,101
Allowance for other funds used during construction	(7,450)	(3,197)
Transfer of long-term purchase commitment to current	7,754	—
Gross additions to other property and investments	794	1,539
Increase (decrease) in other deferred debits	642	(74)
Dividends on preferred stock	3,948	2,575
Dividends on common stock	14,523	10,825
Capital stock expense	375	431
Reduction of long-term debt	4,549	1,000
Increase in bond discount	—	2,196
Other	(129)	903
	155,288	116,299
Decrease in working capital	$ 3,265	$ 29,679

The accompanying notes are an integral part of the consolidated financial statements.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION— (Continued)

For the years ended December 31, 1979 and 1978

	1979	1978
	(In thousands)	
Increase (decrease) in components of working capital:		
Current assets:		
Cash	$ 4,652	$1,685
Restricted cash	—	(6,600)
Accounts receivable	3,002	942
Federal income tax refundable	(3,344)	2,011
Materials and supplies	1,059	203
Fuel	(789)	2,647
Prepayments	(76)	272
Deferred fuel costs	(1,514)	(5,411)
Other	418	(534)
	3,408	(4,785)
Current liabilities:		
Current portion of long-term debt	3,504	1,045
Notes payable to banks	(24,475)	15,735
Notes payable, other	15,290	—
Commercial paper	2,157	6,875
Turbine contract payable	7,754	—
Fuel purchase commitment	(789)	2,647
Accounts payable	1,625	(823)
Customer deposits	402	450
Taxes accrued	704	1,132
Deferred income taxes	(737)	(2,854)
Interest accrued	352	509
Other	886	178
	6,673	24,894
Decrease in working capital	$3,265	$29,679

The accompanying notes are an integral part of the consolidated financial statements.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. Summary of Significant Accounting Policies:

General

The Company maintains its accounts in accordance with the Uniform System of Accounts prescribed for electric utilities by the Federal Energy Regulatory Commission (FERC).

Reclassification

In accordance with the Securities and Exchange Commission Accounting Series Release No. 268 issued July 27, 1979, the Consolidated Balance Sheet at December 31, 1978, has been reclassified to state preferred stock-redemption required and preferred stock-redemption not required, separately.

Principles of Consolidation

The consolidated financial statements include El Paso Electric Company and its wholly-owned subsidiary, Franklin Land & Resources, Inc. All intercompany balances and significant intercompany transactions have been eliminated in consolidation.

Utility Plant

Utility plant and equipment are stated at original cost. The Company provides for depreciation on a straight-line basis at annual rates which will amortize the undepreciated cost of depreciable property over estimated remaining service lives.

The Company charges the cost of repairs and minor replacements to the appropriate operating expense and capitalizes the cost of renewals and betterments. The cost of depreciable plant retired or sold, and the cost of removal, less salvage, is charged to accumulated provision for depreciation.

Inventories

Materials and supplies and fuel inventories are valued at the lower of average cost or market.

Unamortized Capital Stock Expense

Unamortized amounts apply to outstanding issues and are being charged to retained earnings over a ten-year period.

Revenues

Revenues are recognized based on cycle billings rendered to customers monthly. The Company does not accrue revenues in respect to energy consumed but not billed at the end of a fiscal period.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Unamortized Expense, Premium and Discount on Debt

Unamortized amounts apply to outstanding issues and are being amortized ratably over the lives of such issues.

Federal Income Taxes and Investment Tax Credits

Accelerated depreciation of utility plant and amortization of emergency facilities are used for federal income tax reporting purposes which differs from the methods used for financial reporting purposes. Differences in the tax and financial methods of accounting for fuel costs and other capitalized costs also exist. In accordance with regulatory authority requirements, provision has been made in the financial statements for federal income taxes deferred to future years as a result of these items. The Company has not provided deferred taxes on certain other differences between financial and tax reporting, prior to 1979, since such differences were not approved as an expense in rate of return computations by regulatory authorities.

Effective January 1, 1979, in accordance with a Texas rate order, the Company began providing deferred federal income taxes relating to the borrowed portion of AFUDC, to certain capitalized costs, and to all differences between book and tax depreciation for property placed in service after 1978.

Investment tax credits are deferred and amortized to income over the estimated service lives of the related properties.

Pension Plan

The Company has a noncontributory retirement annuity plan (future participation terminable at any time) under a group annuity contract. The pension plan provides annual pensions for regular employees with more than one year of service. The Company's policy is to fund pension costs accrued. Prior service costs are being amortized over a thirty-year period beginning in 1972 and are included in the determination of annual expenses.

Net Income Per Common Share

Net income per common share is computed using the weighted average number of common shares outstanding during the year. Common equivalent shares related to the Amended Employee Stock Purchase Plan are not significant.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

B. Utility Plant:

Electric plant consisted of the following:

	December 31, 1979	December 31, 1978
	(In thousands)	
Intangibles	$ 50	$ 50
Production	131,761	130,714
Transmission	48,668	47,159
Distribution	100,148	92,959
General	9,205	9,324
Plant held for future use	397	397
Construction work in progress	260,419	143,826
Nuclear fuel and other investments	11,135	13,656
Total	$561,783	$438,085

At December 31, 1979 and 1978, a commitment in the amount of approximately $7,754,000 and $7,163,000, respectively, to purchase a turbine from an independent trust no later than June 20, 1980, has been included in construction work in progress. Corresponding amounts have been reflected as a turbine contract payable and as a long-term purchase commitment at December 31, 1979 and 1978, respectively.

During the years ended December 31, 1979 and 1978, interest in the amount of approximately $1,643,000 and $1,098,000, respectively, relative to funds borrowed by a turbine trust and the Company's subsidiary has been capitalized. The borrowed funds at rates ranging from 4-1/4% to 15-1/4% were used to acquire utility plant (construction work in progress and nuclear fuel and other investments). The interest amount has been included in the Consolidated Statement of Income as "Other Interest" with a corresponding amount included in "Other Interest Capitalized." Such interest amounts prior to January 1, 1978, were minimal.

The Company has a 7% undivided interest in Units 4 and 5 of the Four Corners Project located in northwestern New Mexico and a 15.8% undivided interest in Units 1, 2 and 3 of Palo Verde Nuclear Generating Station which are under construction near Phoenix, Arizona. The Company is also constructing transmission facilities related to this station. Participants in the joint plants are responsible for obtaining their respective financing. The extent of Company interests in these facilities, excluding nuclear fuel, is as follows:

	December 31, 1979		December 31, 1978	
	Palo Verde Nuclear Generating Station	Four Corners Project	Palo Verde Nuclear Generating Station	Four Corners Project
	(In thousands)			
Utility plant (in service)		$13,681		$13,391
Accumulated provision for depreciation		(2,712)		(2,362)
Utility plant (under construction)	$241,352	1,453	$130,900	848

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company's direct expenses associated with Four Corners Project are included in the applicable operating expense categories of the Consolidated Statement of Income.

Total depreciation was approximately $8,531,000 in 1979 and $7,616,000 in 1978, of which approximately $286,000 and $255,000, respectively, was applicable to transportation equipment and has been charged to other accounts.

The average annual depreciation rate used by the Company for the years ended December 31, 1979 and 1978, was 2.93%.

C. Common Stock:

Under a shareholder approved employee stock purchase plan qualified employees may purchase shares of the Company's common stock at two specified dates each year for a period ending no later than June 30, 1984. The purchase price is 90% of the average bid price of the stock at the option dates. During 1979 and 1978, 6,717 and 11,120 shares of common stock, respectively, were purchased at an aggregate cost of approximately $63,000 and $111,000, respectively. The cumulative aggregate corresponding fair market values as of the purchase dates were approximately $70,000 and $117,000, in 1979 and 1978, respectively. At December 31, 1979, 66,878 shares were reserved for future purchases under the plan. Proceeds from purchases are credited to common stock and no charges are reflected in income with respect to the plan.

The Company has a Dividend Reinvestment and Stock Purchase Plan which provides holders of its common stock the option to invest cash dividends and/or optional cash payments (up to $3,000 per quarter) in additional shares of the Company's common stock. During 1979 and 1978, 178,652 and 116,904 shares, respectively, were purchased by shareholders who reinvested dividends and invested cash in the amounts of approximately $1,854,000 and $1,263,000, respectively. At December 31, 1979, 332,195 shares were reserved for future purchases under the plan. The purchase price is the average of the last bid and asked price of the stock on the purchase date.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company adopted an employee stock ownership plan in May, 1978, pursuant to which it contributes common stock to the plan for the benefit of employees. The value of such common stock is equal to a specified amount of investment tax credit. The Company reserved 500,000 shares of common stock for issuance under the plan. In October, 1979, the Company contributed 126,633 shares of stock with a market value of approximately $1,287,000 to the plan. In June, 1978, the Company contributed 26,529 shares of stock with a market value of approximately $294,000 to the plan. At December 31, 1979, 346,838 shares were reserved for future contributions under the plan.

During June, 1979, the Company's Restated Articles of Incorporation were amended, increasing the number of authorized shares of common stock to 30,000,000.

Changes in common stock and unamortized capital stock expense were as follows (In thousands, except share amounts):

Description	Common Stock Shares	Common Stock Amount	Unamortized Capital Stock Expense Net*
Balance, December 31, 1977	8,536,818	$ 41,064	($ 496)
Sales of Common Stock	2,654,553	30,205	(292)
Balance, December 31, 1978	11,191,371	71,269	(788)
Sales of Common Stock	3,312,002	35,060	(241)
Balance, December 31, 1979	14,503,373	$106,329	($1,029)

*Capital stock expenses reflected above are stated net of amortization and include expenses of all capital stock issues.

Subsequent to December 31, 1979 (in February 1980), the Company sold 1,500,000 shares for aggregate net proceeds of $13,518,000 before expenses of sale.

Net income applicable to common stock, net income per share of common stock, and weighted average number of common shares outstanding for the year ended December 31, 1979, would have been $19,469,000, $1.34, and 14,502,102, respectively, assuming that the proceeds (before expenses of sale) of $121,374,000 from the sale of first mortgage bonds, preferred stock, common stock and a promissory note during the year and in February, 1980, were used to retire short-term debt outstanding during the year ended December 31, 1979.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

D. Preferred Stock (authorized 1,000,000 shares):

Preferred stock – Redemption required

Following is a summary of outstanding preferred stock – redemption required:

Issue	Stated Value December 31, 1979	Stated Value December 31, 1978	Optional Redemption Price Per Share at December 31, 1979
	(In thousands)		
100,000 Shares $10.75 Dividend	$10,000	$10,000	$110.75
140,000 Shares $ 8.44 Dividend	14,000	14,000	108.44
10,000 Shares $ 8.44 Dividend	1,000		108.44
150,000 Shares $ 8.95 Dividend	15,000		108.95
100,000 Shares $ 9.00 Dividend	10,000		—
	$50,000	$24,000	

The $10.75 preferred shares are entitled to the benefits of an annual sinking fund whereby on January 1 of each year, beginning in 1980, the Company will redeem 4,000 shares at the sinking fund redemption price of $100 per share plus accrued dividends. The $10.75 preferred shares are redeemable at the option of the Company; however, no optional redemption of the shares may be made prior to January 1, 1985, as a part of, or in anticipation of, any refunding involving the issue of indebtedness or preferred stock having an effective interest or dividend cost of less than 10.75% per annum.

The $8.44 preferred shares are entitled to the benefits of an annual sinking fund whereby on October 1 of each year, beginning in 1984, the Company will redeem 4% (and may, at its option, redeem an additional 4%) of the aggregate maximum number of shares outstanding at the sinking fund redemption price of $100 per share plus accrued dividends. The $8.44 preferred shares are redeemable at the option of the Company; however, except as set forth above, no optional redemption of the shares may be made prior to October 1, 1988, as a part of, or in anticipation of, any refunding involving the issue of indebtedness or preferred stock having an effective interest or dividend cost of less than 8.44% per annum.

The $8.95 preferred shares are entitled to the benefits of an annual sinking fund whereby on October 1 of each year, beginning in 1985, the Company will redeem 5% (and may, at its option, redeem an additional 5%) of the aggregate maximum number of shares outstanding at the sinking fund redemption price of $100 per share plus accrued dividends. The $8.95 preferred shares are redeemable at the option of the Company; however, no optional redemption of the shares may be made prior to October 1, 1984, as a part of, or in anticipation of, any refunding involving the issue of indebtedness or preferred stock having an effective interest or dividend cost of less than 8.95% per annum.

Sinking fund requirements for each of the above series are cumulative and, in the event they are not satisfied at any redemption date, the Company is restricted from paying any dividends on its common stock (other than dividends in common stock or other class of stock ranking junior to the preferred stock as to dividends and assets).

The $9.00 preferred shares have no provision for a sinking fund, are not redeemable at the option of the Company, and must be redeemed in full on October 1, 1986 at $100 per share plus accrued dividends. In the event the Company fails to provide sufficient funds for redemption, the Company is restricted from paying any dividends on its common stock (other than dividends in common stock or other class of stock ranking junior to the preferred stock as to dividends and assets).

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The aggregate amounts of the above preferred stock required to be retired for each of the next five years are as follows:

	(In thousands)
1980	$ 400
1981	400
1982	400
1983	400
1984	1,000

Sales of preferred stock – redemption required were as follows:

Description	Shares	Amount (In thousands)
Balance, December 31, 1977	100,000	$10,000
Issuance of Preferred Stock, $8.44 Dividend	140,000	14,000
Balance, December 31, 1978	240,000	24,000
Issuance of Preferred Stock, $8.44 Dividend	10,000	1,000
Issuance of Preferred Stock, $8.95 Dividend	150,000	15,000
Issuance of Preferred Stock, $9.00 Dividend	100,000	10,000
Balance, December 31, 1979	500,000	$50,000

Preferred stock – Redemption not required

Following is a summary of preferred stock which is not redeemable except at the option of the Company:

Issue	Stated Value at December 31, 1979	1978	Optional Redemption Price Per Share at December 31, 1979
	(In thousands)		
15,000 Shares $4.50 Dividend	$ 1,534	$ 1,534	$109.00
15,000 Shares $4.12 Dividend	1,506	1,506	103.98
20,000 Shares $4.72 Dividend	2,001	2,001	104.00
40,000 Shares $4.56 Dividend	4,000	4,000	100.00
100,000 Shares $8.24 Dividend	9,832	9,832	107.52
	$18,873	$18,873	

The $8.24 preferred shares are redeemable at the option of the Company; however, no optional redemption of the shares may be made prior to April 1, 1982, directly or indirectly as part of, or in anticipation of, any refunding involving the issue of the indebtedness or preferred stock having an interest or dividend cost less than the effective dividend cost of the $8.24 preferred stock.

All preferred stock issues (redemption required and redemption not required) are entitled, in preference to common stock, to $100.00 per share, plus accrued dividends, upon involuntary liquidation. All issues except the $9.00 preferred stock are entitled to an amount per share equal to the applicable optional redemption price, plus accrued dividends, upon voluntary liquidation. The $9.00 preferred stock issue is entitled to a fixed price ($109.00 per share at December 31, 1979), plus accrued dividends, upon voluntary liquidation.

There have been no changes in preferred stock – redemption not required during the two years ended December 31, 1979.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

E. Long-Term Debt:

Outstanding long-term debt is as follows:

	December 31, 1979	December 31, 1978	Redemption Price at December 31, 1979
	(In thousands)		
First mortgage bonds:			
2-7/8% Series, due 1980	$ 4,500	$ 4,500	$100.00
3-1/8% Series, due 1984	4,950	4,950	100.85
4-1/4% Series, due 1988	6,100	6,100	101.90
4-5/8% Series, due 1992	10,385	10,385	102.42
6-3/4% Series, due 1998	24,800	24,800	104.19
7-3/4% Series, due 2001	15,838	15,838	106.46
9% Series, due 2004	20,000	20,000	107.04
9.95% Series, due 2004	25,000	—	109.95
10-1/2% Series, due 2005	15,000	15,000	109.84
8-1/2% Series, due 2007	25,000	25,000	108.15
	151,573	126,573	
Unsecured floating rate (15.25% at December 31, 1979) promissory note, due 1984	25,000	—	
4-1/4% pollution control revenue bonds, 1977 Series A, due 1979	—	5,000	
Less funds on deposit with trustee	—	(4,000)	
Other, 8.8125%, due in installments through 1998	2,124	2,169	
	178,697	129,742	
Current maturities of long-term debt	(4,549)	(1,045)	
Unamortized premium and discount	(2,427)	(2,545)	
	$171,721	$126,152	

Scheduled maturities of long-term debt at December 31, 1979, are as follows (in thousands):

1980	$ 4,549
1981	54
1982	59
1983	64
1984	30,020
Thereafter	143,951
	$178,697

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company's indenture of mortgage provides for sinking and improvement funds. For each series other than the 9.95% series, the Company is required to make annual payments to the trustee equivalent to 1% ($1,275,000 at December 31, 1979 and 1978) of the greatest aggregate principal amount of such series outstanding prior to a specified date. The Company has generally satisfied the 1% requirement by relinquishing the right to use a net amount of additional property for the issuance of bonds or by purchasing bonds in the open market and expects to continue this practice in the future. With respect to the 9.95% series, commencing April 30, 1985, the Company will be required to make annual cash payments to the trustee equivalent to 4-1/4% of the greatest aggregate principal amount of such series outstanding at any one time prior to a specified date. The 4-1/4% cash payment must be applied to redeem bonds of the 9.95% series at 100% of the principal amount thereof plus accrued interest.

The premiums reflected in the redemption prices shown above continue at reduced amounts in future years, finally resulting in each case in redemption at par at maturity.

Substantially all of the Company's utility plant is subject to a lien under the indenture of mortgage collateralizing the Company's bonds.

In accordance with certain provisions of the indenture covering the first mortgage bonds, payment of cash dividends on common stock is restricted to an amount equal to retained earnings accumulated after December 31, 1966, plus $4,100,000. Retained earnings in the amount of approximately $27,800,000 is unrestricted as to the payment of cash dividends at December 31, 1979.

The funds on deposit with a trustee ($4,000,000) at December 31, 1978, represent a portion of the proceeds from pollution control revenue bonds issued in November, 1977. The bonds were redeemed in November, 1979.

F. Notes Payable and Commercial Paper:

Short-term notes at December 31, 1979, consisted of $34,332,000 of commercial paper with an effective weighted average interest rate of 13.9%, $2,125,000 of notes payable to banks with an effective weighted average interest rate of 14.7%, and $15,290,000 of notes payable, other, with an effective weighted average interest rate of 13.1%.

Short-term notes at December 31, 1978, consisted of $32,175,000 of commercial paper with an effective weighted average interest rate of 10.4% and $26,600,000 of notes payable to banks with an effective weighted average interest rate of 10.6%.

The Company and its subsidiary have informal lines of credit with various lenders. Certain of these arrangements provide for the maintenance of compensating balances for the available lines of credit and the loans outstanding. At December 31, 1979 and 1978, the lines of credit available under these arrangements totaled $104,336,000 (including subsidiary lines of $17,625,000 not guaranteed by the Company) and $67,925,000 (including subsidiary lines of $10,925,000 not guaranteed by the Company), respectively. Average bank balances of approximately $4,710,000 and $2,550,000 were required to be maintained as compensating balances at December 31, 1979 and 1978, respectively, in connection with the informal lines of credit.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The maximum and average amounts of aggregate short-term borrowings outstanding at any month-end during the year ended December 31, 1979, were $74,767,000 and $59,717,000, respectively, and for the year ended December 31, 1978, were $58,775,000 and $43,054,000, respectively. The weighted average interest rate was 10.9% and 7.4% during the years ended December 31, 1979 and 1978, respectively, and was calculated by dividing actual interest expense by the average month-end balances outstanding during the related period.

Through December 31, 1980, the FERC has authorized the Company to incur short-term debt (in the form of promissory notes or commercial paper) in an amount not to exceed $130,000,000 outstanding at any one time. The interest rates on the notes are to be at the prime rate in effect at the time of issuance, plus in some cases, provisions for compensating balances of 20% under certain conditions. The net proceeds from the issuance of the short-term debt are to be used for construction expenditures.

G. Federal Income Taxes:

The provisions for deferred federal income taxes, which arise from timing differences between financial and tax reporting, are as follows:

	Years Ended December 31,	
	1979	1978
	(In thousands)	
Tax effect of:		
Depreciation differences	$1,769	$1,572
Deferred fuel costs	(1,074)	(2,597)
Allowance for borrowed funds used during construction	4,023	—
Other costs capitalized	733	—
Amortization related to emergency facilities	(111)	(111)
Deferred rate case expense and other	798	(364)
	$6,138	($1,500)

Effective January 1, 1979, in accordance with a Texas rate order, the Company began providing deferred federal income taxes applicable to the allowance for borrowed funds used during construction, to other costs capitalized and to all differences between book and tax depreciation for property placed in service after 1978. Accordingly, additional deferred taxes of approximately $4,828,000 are reflected in deferred tax expense for the year ended December 31, 1979.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Federal income tax provisions are less than the amounts computed by applying the statutory rate to income before federal income taxes. Details are as follows:

	Years Ended December 31, 1979	1978
	(In thousands)	
Tax computed at statutory rate	$16,062	$10,264
Decreases due to:		
Allowance for funds used during construction	(3,427)	(3,602)
Excess of straight-line tax depreciation over book depreciation	(176)	(348)
Amortization of deferred investment tax credit	(296)	(398)
Other	(435)	(556)
Total federal income tax expense	$11,728	$ 5,360
Effective federal income tax rate	33.6%	25.1%

Total federal income tax expense is as follows:

	Years Ended December 31, 1979	1978
	(In thousands)	
Federal income tax, current (credit)	$ 1,238	($2,617)
Income taxes associated with other income	269	463
Total current	1,507	(2,154)
Deferred federal income tax (credit)	6,138	(1,500)
Deferred investment tax credit	4,379	9,412
Amortization of deferred investment tax credit	(296)	(398)
	$11,728	$5,360

At December 31, 1979, the Company has available for federal income tax purposes an investment tax credit carryforward of approximately $7,000,000 expiring in 1986.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

H. Commitments and Contingencies:

The Company has a 15.8% interest in three units of a nuclear plant and related transmission lines and switchyard presently under construction. The costs to be incurred by the Company at December 31, 1979, are approximately $612,600,000, including approximately $169,700,000 of AFUDC. The Company is also committed at December 31, 1979, for construction of pollution control facilities in the amount of approximately $15,200,000, including approximately $2,600,000 of AFUDC. The above amounts were computed assuming an estimated average annual inflation rate of 7%.

In January, 1979, the Company entered into an agreement with an independent trust whereby the Company sold to the trust, at cost, substantially all of its nuclear fuel. Under the trust agreement the Company has the option of either repurchasing the fuel from the trust or leasing the heat generated by the fuel. Management of the Company intends to enter into a basic heat supply contract whereby title to the fuel remains with the trust and the Company makes lease payments for the heat generated. Based on this intention and in accordance with industry practice, the nuclear fuel and related liability are not included in the accompanying balance sheet. At December 31, 1979, the trust has incurred cumulative costs of approximately $8,200,000. The Company expects that fuel costs incurred will be recouped at the time the fuel is used. The Company is committed to reimburse the trust for its cash investment in nuclear fuel, not expected to exceed a maximum cash amount of $68,000,000 during the ten-year period ending December 31, 1989, as well as for interest and other carrying costs of the trust.

The Company's fuel supply arrangements include short-term commitments under a fuel supply arrangement entered into in 1977 with a trust, whereby the Company concurrently assigned its principal long-term fuel supply contract to the trust and agreed to purchase all fuel oil delivered to the trust by the fuel supplier. Payments to the trust for fuel oil purchases consist of the trust's cost of oil determined on an average cost basis plus related administrative and carrying costs. For financial reporting purposes, purchases of the trust are assumed to have been made on behalf of the Company. Accordingly, the balance sheet at December 31, 1979 and 1978, includes approximately $7,958,000 and $8,747,000, respectively, recorded as fuel and fuel purchase commitment, representing the Company's commitment to purchase the trust's fuel oil inventory as of those dates.

The Company's operations are subject to environmental protection measures imposed under federal and state laws and regulations.Management does not believe that the impact of any of these matters will have a material adverse effect on the financial statements.

The Company's rates, including fuel adjustment clauses, are subject to the jurisdiction of local, state, and federal authorities. The Company believes that regulatory agencies will continue to allow rate increases designed to allow utilities to recover costs and a reasonable return on investment.

Revenues for 1979 and 1978 include approximately $623,000 and $635,000, respectively, subject to refund pending final determination by the FERC.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

I. Allowance for Funds Used During Construction:

The applicable regulatory uniform system of accounts provides for "allowance for funds used during construction" ("AFUDC") which is defined as an amount which includes the net cost during a period of construction of borrowed funds used for construction purposes plus a reasonable rate on other funds when so used. While AFUDC results in an increase in utility plant under construction for ratemaking purposes with a corresponding credit to income, it is not a current cash item. AFUDC is realized in cash after the related plant is placed in service through the allowance for depreciation charges based on the total cost of the plant, including AFUDC.

The amount of AFUDC is determined by applying an accrual rate to the balance of certain utility plant additions. The Company used an accrual rate of 9-1/2% in 1978. During 1979, the Company changed the rate used to calculate AFUDC from 9-1/2% to 11%, effective as of January 1, 1979. In this connection, the FERC promulgated procedures for the computation (a prescribed formula) of the accrual rate which became effective in 1977. The rates used by the Company do not exceed those permitted under the prescribed FERC formula.

The increase in the AFUDC rate as of January 1, 1979, increased net income by approximately $1,659,000 and net income per share by approximately $.13 for the year ended December 31, 1979. The AFUDC rate is reviewed quarterly and adjustments, if any, are applied to the full year.

J. Pension Plan:

The Company had $751,000 of pension expense in 1979 and $680,000 in 1978. As of July 1, 1978, date of the most current actuarial valuation, assets of the pension fund exceeded vested benefits by approximately $677,000 and unfunded prior service benefits were estimated to be approximately $3,500,000.

K. Supplementary Profit and Loss Information:

Supplementary profit and loss information with respect to operating expenses is as follows:

	Years Ended December 31, 1979	1978
	(In thousands)	
Taxes, other than federal income taxes:		
Municipal and state property	$ 6,653	$ 4,654
Occupancy and street rental	1,964	1,701
State gross receipts	2,029	1,741
Other	1,109	2,473
Total	$11,755	$10,569
Charged to:		
Taxes, other	$10,114	$ 9,231
Utility plant and other accounts	1,641	1,338
Total	$11,755	$10,569

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Expenditures for rents, royalties, advertising and development costs individually did not exceed 1% of total revenues and hence are not presented.

L. Quarterly Financial Summary (Unaudited):

The following table sets forth the quarterly financial summary of the Company for the years ended December 31, 1979 and 1978:

(In Thousands of Dollars Except for Per Share Data)
(All Quarterly Data is Unaudited)

1979	Operating Revenues	Operating Expenses	Operating Income	Net Income	Net Income Applicable To Common Stock	Net Income Per Common Share
1st quarter	$36,873	$32,119	$4,754	$3,976	$3,085	$.25
2nd quarter	37,147	31,564	5,583	5,334	4,441	.35
3rd quarter	45,604	37,927	7,677	7,705	6,801	.50
4th quarter	40,088	34,033	6,055	6,175	4,915	.34
1978						
1st quarter	31,418	27,142	4,276	2,812	2,236	.24
2nd quarter	36,219	30,899	5,320	3,883	3,307	.33
3rd quarter	37,787	31,470	6,317	5,133	4,556	.43
4th quarter	31,132	26,596	4,536	4,196	3,350	.30

M. Replacement Cost Information (Unaudited):

The impact of inflation experienced in recent years has resulted in replacement costs of productive capacity that are significantly greater than the historical costs of such assets reported in the Company's financial statements. The Company's ability to maintain its productive capacity in the future will be contingent upon its ability to finance the needed additions. This, in turn, will depend on the Company's ability to obtain adequate and timely rate relief. The Company retained Stone & Webster Appraisal Corporation of Boston, Massachusetts ("Stone & Webster Appraisal") to determine the approximate replacement cost of the Company's productive capacity.

The replacement cost information does not purport to represent the current value or reproduction costs of the assets or the amounts which could be realized if the assets were sold. Rather, replacement cost generally represents the estimated amount that would be required to replace, at today's prices, the productive capacity of certain of the Company's existing assets with assets of a modern type including additional pollution control equipment presently required under environmental regulations. Such replacement would result in changes in fuel, operation and maintenance cost which are not reflected in the data submitted.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The replacement costs reflected in the table below were determined on the basis of replacing existing capacity (which uses gas, oil and coal as fuels) with capacity fueled by oil and coal. Due to federal legislation in connection with a national energy policy, replacement of existing capacity with capacity fueled by oil may no longer be a viable alternative. To the extent existing capacity must be replaced by capacity using coal or nuclear fuel, replacement costs could be expected to increase substantially.

The difference between historical and replacement cost of net plant investment does not represent additional book value for the Company's common stock; instead, it indicates the capital funds (in excess of booked depreciation and other prior capital provisions) that may have to be provided to replace existing service capacity of the plant of the Company.

The Company's business is subject to the jurisdiction of regulatory commissions in the determination of fair rates of return on its investment in utility plant. Under current ratemaking policy, the Company recovers, through future depreciation charges, the historical dollars invested in productive capacity. The ratemaking process does not allow the Company to recover the excess of replacement cost over historical cost. However, at such time as amounts are actually expended to replace existing assets, such amounts will be considered in determining the Company's rate base for purposes of ratemaking.

The Company believes that the difference between depreciation based on historical cost and depreciation based on estimated replacement cost, which difference is not deductible in determining income tax expense, is not truly an additional amount of depreciation expense. Rather, it is a measure of the extent to which the Company should be making provision in the current year for replacement of its existing plant, assuming no growth in demands for service and no further inflation in costs.

The consolidated replacement cost information on a comparative basis with historical cost is shown in the tabulation below as of December 31, 1979 and 1978 (amounts in thousands):

	1979		1978	
	Estimated Replacement Cost	Actual Historical Cost	Estimated Replacement Cost	Actual Historical Cost
Plant investment subject to replacement cost disclosure *	$1,043,102	$561,783	$854,720	$438,085
Accumulated depreciation	203,860	76,053	171,808	68,672
Net plant investment	$ 839,242	$485,730	$682,912	$369,413
Depreciation expense for the year	$ 20,205	$ 8,531	$ 18,089	$ 7,616

*Amounts exclude nonutility plant of approximately $2,357,000 and $1,563,000, respectively, and include land, intangible assets, construction work in progress, and nuclear fuel and other investments at original cost of approximately $275,712,000 and $160,750,000 as of December 31, 1979 and 1978, respectively.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

N. Estimated Effect of Inflation (Unaudited):

The Financial Accounting Standards Board issued Statement No. 33 "Financial Reporting and Changing Prices" to provide estimates of the impact from inflation on a business' operations. The schedules below are intended to indicate the effect on the Company from general inflationary pressures as measured by the Consumer Price Index (CPI). Due to estimating techniques and certain judgemental decisions, the information should be viewed as only an approximation of inflation's effect.

Constant dollar amounts represent historical costs stated in dollars of equal purchasing power, as measured by the Consumer Price Index for all Urban Consumers. The cost of plant was restated to average 1979 dollars and depreciation expense was calculated by applying the Company's depreciation rate to the restated amounts.

As prescribed in Statement 33 income taxes were not adjusted.

Fuel used in generation has not been restated from historical cost amounts nor have inventories. Fuel costs are recoverable currently through the operation of fuel adjustment clauses and inventory turnover periods are relatively short. In accordance with FASB Statement No. 33, other items of income and expense have not been restated.

The regulatory commissions having jurisdiction over the Company's rates allow for the recovery of the historical cost of plant through depreciation. The restated cost of plant is not presently recoverable. Therefore, the difference between historical plant cost and restated plant cost is shown below as a reduction to net recoverable cost. The reduction to recoverable cost should be offset by the gain from the decline in purchasing power of net amounts owed.

During inflationary periods, holders of monetary assets suffer a loss of general purchasing power while holders of monetary liabilities experience a gain. The gain from the decline in purchasing power shown below is attributable to the substantial amount of debt used to finance property, plant and equipment. Since the depreciation on plant is limited to the recovery of historical costs, the Company does not have the opportunity to realize a holding gain on debt and is limited to the recovery only of the embedded cost of debt capital.

EL PASO ELECTRIC COMPANY AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

SUPPLEMENTARY STATEMENT OF INCOME FROM OPERATIONS ADJUSTED FOR CHANGING PRICES (Unaudited)

	Year Ended December 31, 1979 (Thousands of Dollars) Conventional Historical Cost	Constant Dollar Average 1979 Dollars
Operating Revenues	$159,712	$159,712
Fuel Purchased and Interchanged Power	78,138	78,138
Other Operating and Maintenance Expenses	37,801	37,801
Depreciation	8,245	15,614
Federal Income Tax	11,459	11,459
Interest Expense	8,621	8,621
Other Income	(7,742)	(7,742)
	136,522	143,891
Income From Operations	$ 23,190	$ 15,821*
Net Income Per Share of Common Stock	$1.45	$ .90
Net Assets at Year End at Net Recoverable Amount		$208,321
Reduction of Plant to Net Recoverable Cost		($45,674)*
Gain From Decline in Purchasing Power of Net Amounts Owed		29,996
Difference		($15,678)

* Inclusion of the reduction to net recoverable cost in income from operations produces a loss of $29,853.

FIVE YEAR COMPARISON OF SELECTED FINANCIAL DATA AVERAGE 1979 CONSTANT DOLLARS (Unaudited)

Years Ended December 31,	1979	1978	1977	1976	1975
Operating Revenues (Thousands)					
Actual	$159,712	$136,556	$112,339	$111,188	$ 91,461
1979 Dollars	159,712	151,931	134,559	141,773	123,348
Cash Dividends Per Common Share					
Actual	$1.07	$1.02	$ .99	$ .95	$ .91
1979 Dollars	$1.07	$1.13	$1.19	$1.21	$1.23
Year-End Market Price Per Common Share					
Actual	$9.38	$10.88	$12.00	$12.00	$10.38
1979 Dollars	$8.87	11.66	14.02	14.97	13.57
Average Consumer Price Index	217.4	195.4	181.5	170.5	161.2

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Shareholders and Board of Directors
El Paso Electric Company

We have examined the consolidated balance sheet of El Paso Electric Company and Subsidiary at December 31, 1979 and 1978, and the related consolidated statements of income, retained earnings and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the consolidated financial position of El Paso Electric Company and Subsidiary at December 31, 1979 and 1978, and the consolidated results of operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

COOPERS & LYBRAND

Dallas, Texas
February 22, 1980

SUMMARY OF OPERATING DATA

	1979	1978	1977
Population served at retail, estimated (a)	554,000	544,000	532,000
Number of Customers:			
Residential	157,601	150,739	143,645
Commercial and industrial, small	15,791	15,381	14,518
Commercial and industrial, large	44	47	46
Other	1,875	1,842	1,715
Total	175,311	168,009	159,924
Annual system peak load, net kilowatts	688,000	690,000	657,000
Output, net generated and purchased, thousand kilowatt-hours:			
Steam	3,771,043	3,673,685	3,475,753
Purchased and interchanged	(119,166)	(84,609)	(3,574)
Total (b) (c)	3,651,877	3,589,076	3,472,179
Sales of electricity, thousands of dollars:			
Residential	$ 52,899	$ 44,178	$ 34,484
Commercial and industrial, small	46,741	39,780	33,583
Commercial and industrial, large	26,402	22,402	17,666
Other	32,577	29,289	25,581
Total	$ 158,619	$ 135,649	$ 111,314
Sales, thousand kilowatt-hours:			
Residential	937,858	907,956	874,140
Commercial and industrial, small	949,514	913,038	902,699
Commercial and industrial, large	682,163	650,542	617,955
Other	854,749	849,113	847,930
Total (b) (c)	3,424,284	3,320,649	3,242,724
Average annual use per residential customer, kwh	6,072	6,153	6,261
Average annual revenue per residential customer	$ 342.49	$ 299.40	$ 246.99
Average revenue per kwh sold, cents:			
Residential (d)	5.64	4.87	3.94
Commercial and industrial, small (d)	4.92	4.36	3.72
Commercial and industrial, large (d)	3.87	4.14	3.47
Average revenue per kwh; total sales (d)	4.63	4.09	3.45
Electric line, pole miles:			
Over 15,000 volts	2,070	1,999	1,811
Less than 15,000 volts (e)	2,794	2,759	2,755
Total	4,864	4,758	4,566
Total employees	965	908	838

(a) Restated as a result of 1970 census.

(b) Differences between total output and total sales represent company use and losses.

(c) In addition to the Company's 345 kv transmission line between El Paso and Albuquerque, the company system is interconnected at Las Cruces, New Mexico, with Public Service Company of New Mexico; Community Public Service Company, Plains Electric Generation and Transmission Cooperative, Inc., and Elephant Butte Generating Station through the facilities of the United States Bureau of Reclamation under a pool agreement.

(d) Includes adjustments under existing fuel clauses.

(e) Includes small amount of line on poles owned by telephone company.

1976	1975	1974	1973	1972	1971	1970
520,000	505,000	495,000	485,000	475,000	465,000	450,000
135,344	130,010	126,760	123,653	119,170	114,640	110,308
14,203	13,294	13,163	12,816	12,333	11,666	11,279
39	32	29	27	27	23	21
1,748	1,663	1,545	1,445	1,351	1,255	1,228
151,334	144,999	141,497	137,941	132,881	127,584	122,836
677,000	640,000	638,000	618,000	543,400	500,700	469,100
3,501,416	3,433,698	3,369,606	3,450,021	3,075,013	2,705,160	2,506,048
51,013	15,837	(13,709)	(180,767)	(112,435)	(43,375)	360
3,552,429	3,449,535	3,355,897	3,269,254	2,962,578	2,661,785	2,506,408
$ 31,415	$ 27,080	$ 20,126	$ 16,749	$ 15,133	$ 14,081	$ 13,099
33,628	28,870	19,192	14,942	12,948	11,515	10,336
15,709	11,816	7,824	6,061	5,231	4,517	4,194
29,537	22,880	15,595	11,416	9,696	8,565	8,155
$ 110,289	$ 90,646	$ 62,737	$ 49,168	$ 43,008	$ 38,678	$ 35,784
816,169	782,285	765,636	755,701	694,855	643,313	598,240
929,556	909,967	853,960	799,997	696,584	610,876	540,529
582,125	513,637	508,482	536,754	487,945	440,568	426,177
1,030,812	1,006,311	980,175	958,252	853,978	758,769	763,597
3,358,662	3,212,200	3,108,253	3,050,704	2,733,362	2,453,526	2,328,543
6,193	6,097	6,116	6,211	5,948	5,718	5,499
$ 238.36	$ 211.04	$ 160.72	$ 137.59	$ 129.53	$ 125.16	$ 120.39
3.85	3.46	2.63	2.22	2.18	2.19	2.19
3.62	3.17	2.25	1.87	1.86	1.89	1.91
2.70	2.30	1.54	1.13	1.07	1.03	.98
3.30	2.82	2.02	1.61	1.57	1.58	1.54
1,759	1,706	1,647	1,581	1,539	1,503	1,442
2,727	2,691	2,673	2,616	2,565	2,507	2,457
4,486	4,397	4,320	4,197	4,104	4,010	3,899
816	778	726	704	659	644	629

SUMMARY OF OPERATIONS

(Thousands of Dollars) Year Ended December 31	1979	1978	1977
Operating revenues	$159,712	$136,556	$112,339
Fuel	81,669	73,447	59,442
Operation and maintenance	24,156	21,171	16,685
Depreciation (a)	8,245	7,361	6,498
Taxes	21,573	14,128	12,377
Other income	(7,742)	(3,688)	(1,689)
	127,901	112,419	93,313
Income before interest charges	31,811	24,137	19,026
Total interest charges	8,621	8,113	7,604
Income before cumulative effect on prior years of change in accounting method	23,190	16,024	11,422
Cumulative effect to January 1, 1974 of change in accounting for fuel costs, net of related income taxes ($912,000)			
Net income	$ 23,190	$ 16,024	$ 11,422
Earnings per share of common stock, based on weighted average number of shares outstanding during each year:			
Income applicable to common stock before cumulative effect of change in accounting method	$ 1.45	$ 1.30	$ 1.11
Cumulative effect to January 1, 1974, of change in accounting for fuel costs			
Net income applicable to common stock	$ 1.45	$ 1.30	$ 1.11
Pro forma amounts assuming the new method of accounting for fuel costs is applied retroactively (b):			
Net income applicable to common stock			
Earnings per share			
Dividends paid per share on common stock	$ 1.07	$ 1.02	$ .99
Electric Plant	$561,783	$438,085	$338,598

(a) Does not include depreciation on automobiles and trucks, which was allocated to other accounts.

(b) The effect of the accounting change in years prior to January 1, 1971, is not significant.

	1976	1975	1974	1973	1972	1971	1970
	$111,188	$ 91,461	$ 63,072	$ 49,483	$ 43,284	$ 38,919	$ 36,026
	53,154	44,714	24,914	15,766	10,951	8,974	7,330
	17,954	14,516	11,463	8,160	8,101	7,717	7,149
	6,233	5,506	4,345	4,102	3,776	3,509	3,256
	15,727	11,197	9,809	9,573	9,279	8,151	8,194
	(838)	(1,423)	(770)	(84)	(668)	(699)	(393)
	92,230	74,510	49,761	37,517	31,439	27,652	25,536
	18,958	16,951	13,311	11,966	11,845	11,267	10,490
	7,442	6,853	5,280	3,962	3,591	3,450	3,073
	11,516	10,098	8,031	8,004	8,254	7,817	7,417
			988				
	$ 11,516	$ 10,098	$ 9,019	$ 8,004	$ 8,254	$ 7,817	$ 7,417
	$ 1.29	$ 1.30	$ 1.19	$ 1.19	$ 1.22	$ 1.16	$ 1.10
			.15				
	$ 1.29	$ 1.30	$ 1.34	$ 1.19	$ 1.22	$ 1.16	$ 1.10
				$ 8,270	$ 8,035	$ 7,481	
				$ 1.29	$ 1.25	$ 1.17	
	$ .95	$ .91	$ .88	$ .86	$ .83	$ .80	$ .76
	$274,502	$250,375	$227,196	$185,058	$174,485	$166,275	$150,859

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE CONSOLIDATED STATEMENT OF INCOME

The factors discussed in the following summary of period to period changes, which may not be indicative of future operations or earnings, have had an effect upon the Company's results of operations during the years ended December 31, 1979 and 1978 (in thousands, except for per share data).

	1979 Increase (Decrease) Over 1978		1978 Increase Over 1977	
Operating revenues	$23,156	17.0%	$24,217	21.6%
Operating expenses	19,536	16.8%	21,105	22.2%
Operating income	3,620	17.7%	3,112	18.0%
Allowance for funds used during construction:				
Other	4,253	133.0%	1,597	99.8%
Borrowed	4,438	103.0%	2,196	104.0%
Other income	(199)	(40.5%)	402	451.7%
Interest charges:				
Long-term debt	2,112	22.3%	1,316	16.1%
Other	2,834	96.3%	1,389	89.4%
Net income	7,166	44.7%	4,602	40.3%
Preferred dividend requirements	1,373	53.3%	538	26.4%
Net income per share	.15	11.5%	.19	17.1%
Weighted average number of common shares outstanding	2,919	28.2%	1,845	21.7%

Operating Revenues

Operating revenues increased in 1979 over 1978 principally as a result of an increase in the average base rate (calculated without giving effect to the recovery of fuel costs). The average base rate for 1979 was .3¢ per kilowatt-hour higher than it was in 1978. Base rates, fuel (collected both in base rates and through fuel adjustment clauses) and volume accounted for approximately 62%, 29% and 9%, respectively, of the total 17.0% increase in revenues in 1979 over 1978.

Operating revenues increased in 1978 over 1977 partially as a result of increased base rates (calculated without giving effect to the recovery of fuel costs). Base rates for 1978 were approximately .3¢ per kilowatt-hour higher than those in 1977. Base rates, fuel (collected both in base rates and through fuel adjustment clauses) and volume accounted for approximately 45%, 50% and 5%, respectively, of the total 21.6% increase in revenues in 1978 over 1977.

Operating Expenses

Increases in operating expenses for 1979 over 1978 were due primarily to increases in fuel expense and federal income tax provisions. Escalations in fuel cost accounted for approximately 42% of the total 16.8% increase, while federal income tax increases contributed 34%. Taxes increased in 1979 over 1978 partially due to the presence of tax credits in 1978 not present in 1979 and the deferral of taxes on allowance for borrowed funds used during construction (ABFUDC) which began in January, 1979.

Increases in operations and maintenance expense (23% of the increase) were due primarily to inflationary pressure on wages, employee benefits, materials and other costs.

Increased operating expenses in 1978 over 1977 were due principally to escalating fuel costs and increases in the aggregate costs of operation, maintenance and depreciation. Such costs accounted for approximately 92% of the total increase. The escalating fuel costs accounted for approximately 66% of the total increase. Increased operations expense (18% of the increase) was due to inflationary pressure on wages, employee benefits, materials and other costs. Increased depreciation expense, which accounted for approximately 4% of the increase, was due to increases in depreciable property together with increased average annual rates in 1978. Increases in federal income taxes accounted for approximately 2% of the increase, while other taxes contributed 7% toward the total increase.

Operating Income

Increases in operating income are directly related to changes in operating revenues and operating expenses in their respective periods. (See the captions "Operating Revenues" and "Operating Expenses" above.)

Allowance for Funds Used During Construction

AFUDC increased in 1979 over 1978 and in 1978 over 1977 due to increased construction expenditures principally associated with the Palo Verde Station as well as increased accrual rates. The Company changed its accrual rate from 9-1/2% to 11% effective January 1, 1979, and from 7-1/2% to 9-1/2% effective January 1, 1978.

AFUDC amounted to 63% and 56% of net income applicable to common stock during the years ended December 31, 1979 and 1978. The 1979 AFUDC contribution to net income is net of the effect of deferred federal income taxes on the borrowed portion of AFUDC.

Other Income

Other income changed in each comparable period primarily as a result of fluctuations in interest income.

Interest Charges

Interest on long-term debt increased in all periods due to the issuance of additional first mortgage bonds and a long-term promissory note during the periods. The changes in other interest in 1979 and 1978 reflect increased short-term borrowing and higher prevailing interest rates in both years.

Net Income Per Share

Changes in net income per share are the result of fluctuations in net income, increases in preferred dividend requirements, and increases in common shares outstanding during the periods.

Annual Meeting of Shareholders

All shareholders are invited to attend the 1980 Annual Meeting of Shareholders Monday, May 19, 1980 at 10 a.m. El Paso time, in the Oleander Room of the Rodeway Inn, 6201 Gateway West, El Paso, Texas.

Proxies for the meeting will be solicited by the Board of Directors in a communication to be mailed in early April. This Annual Report is not a part of such proxy solicitation and is not intended to be used as such.

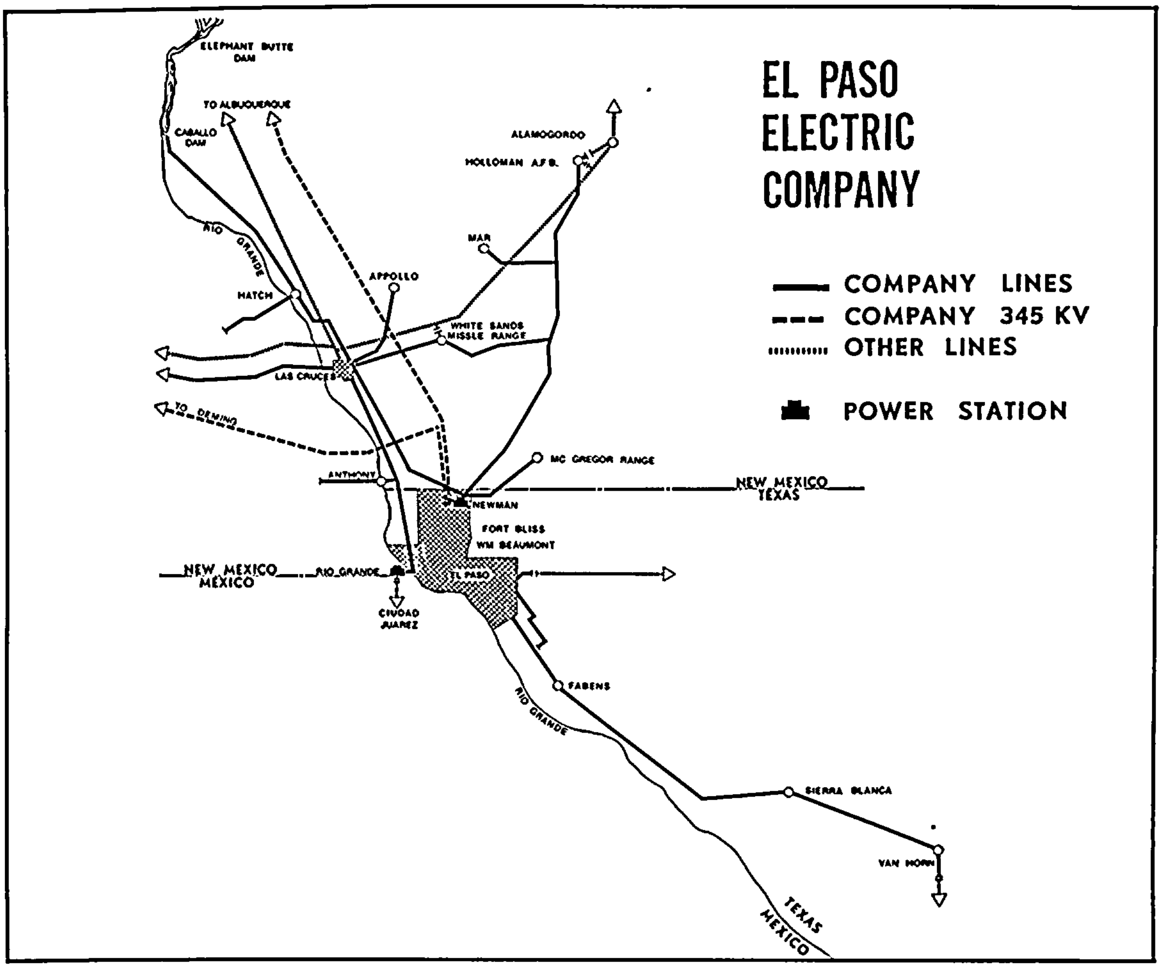
A copy of the Company's most recent 10-K Report, including the financial statements and schedules thereto, filed by El Paso Electric Company with the Securities and Exchange Commission, will be made available to Shareholders without charge upon written request to:
Theta S. Fields, Secretary
El Paso Electric Company
Post Office Box 982
El Paso, Texas 79960

Common Stock Shareholders

The Common Stock of the Company is held in every state of the union, the District of Columbia, some U.S. territories and many foreign countries. The number of Shareholders increased from 25,633 in 1978 to 32,995 in 1979. Many of our customers and other persons in the Southwest are Shareholders as evidenced by the 5,874 Shareholders in Texas and New Mexico who own 19 percent of the outstanding shares. Our records show that 82 percent of the Company's shareholders own less than 500 shares each.

Transfer Agents
Irving Trust Company
One Wall Street
New York, New York 10015
(Common and Preferred Stock)

The State National Bank of El Paso
Post Office Box 1072
El Paso, Texas 79958
(Common Stock Only)



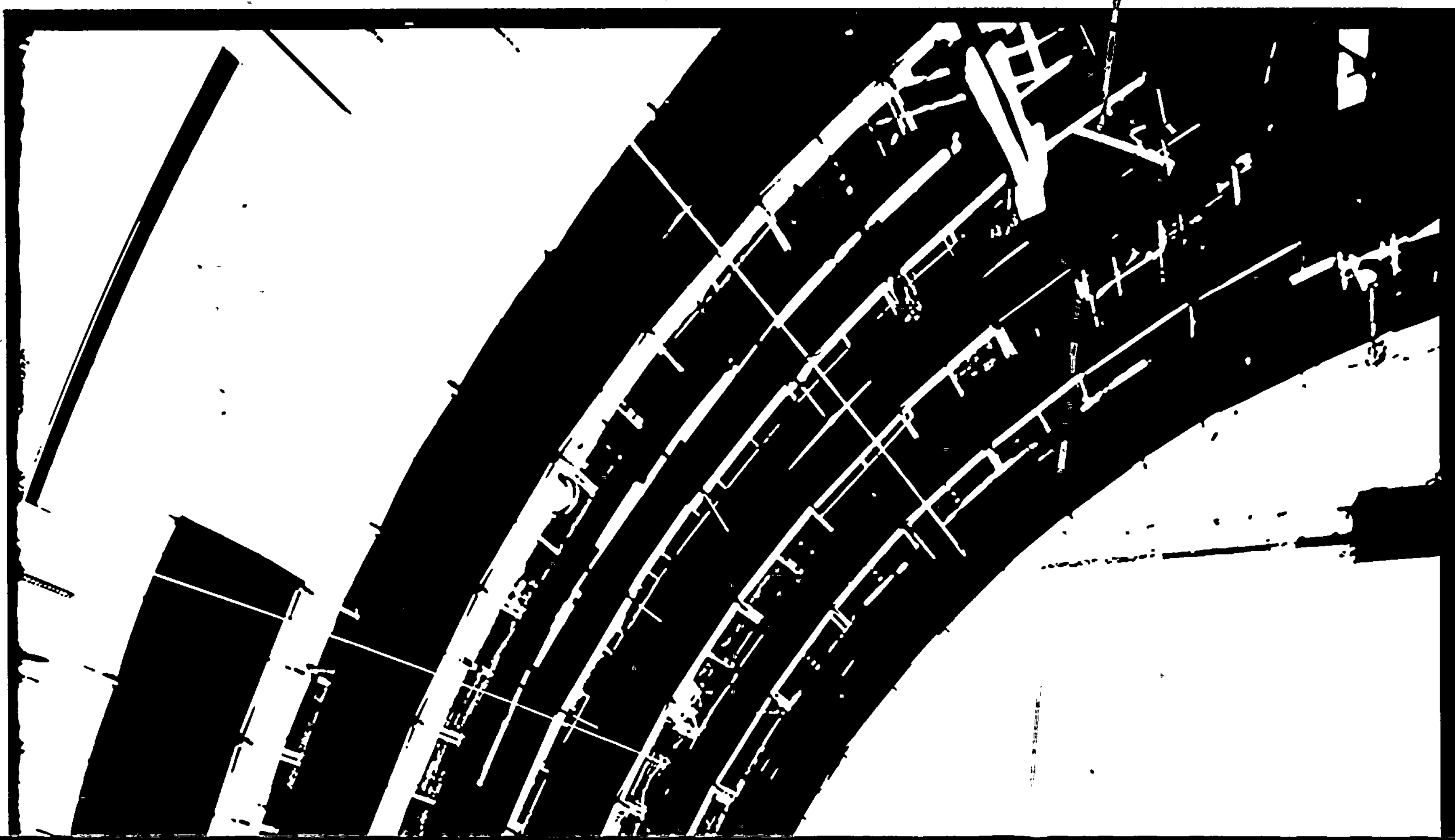
Service Area

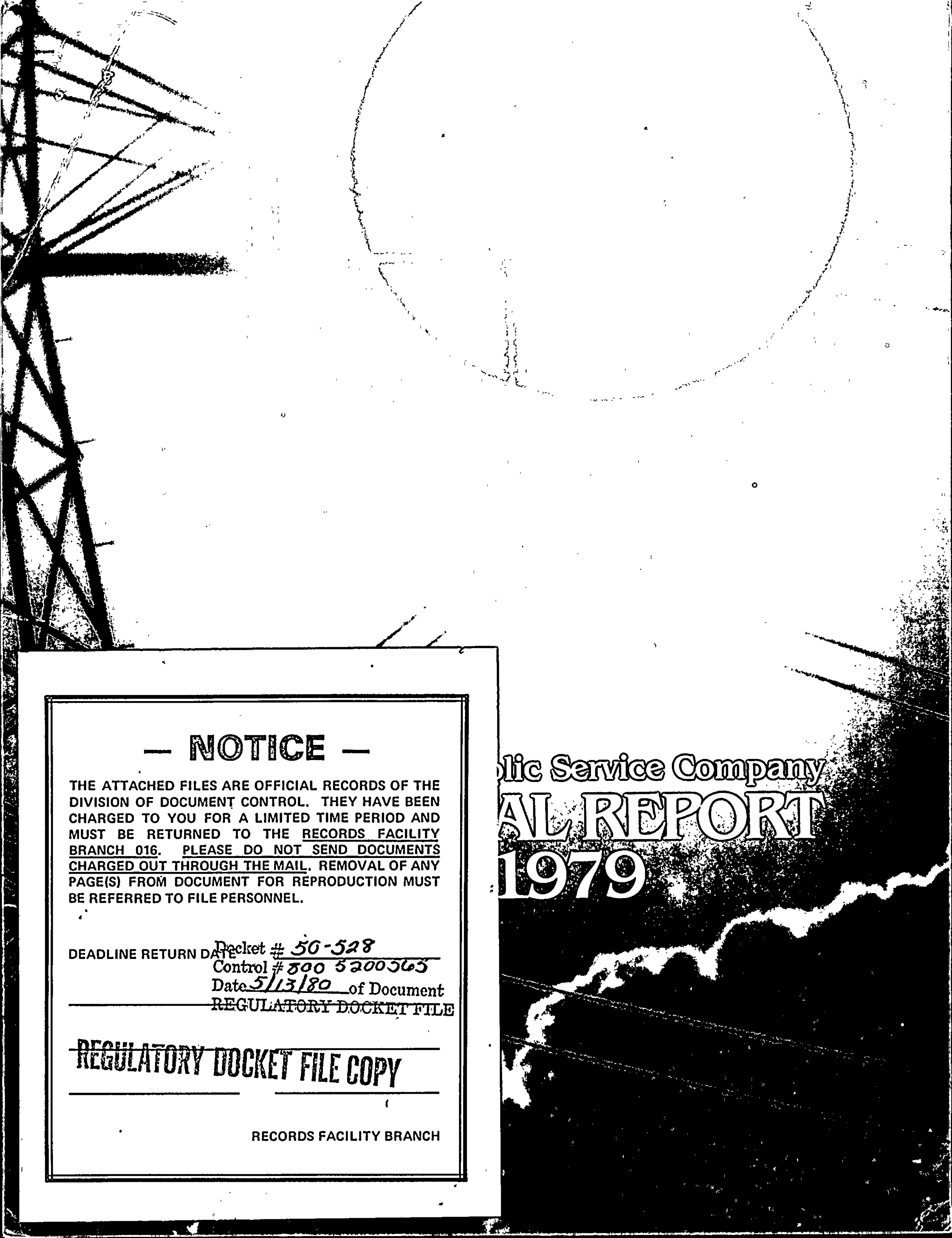
El Paso Electric is an investor-owned, tax-paying electric utility operating in Texas and New Mexico. The Company is engaged in the generation, transmission, distribution and sale of electric energy. El Paso Electric serves approximately 175,000 customers in West Texas and South Central New Mexico in a service area of approximately 10,000 square miles. The service area extends from the Caballo Dam in New Mexico southeasterly to Van Horn, Texas.

El Paso Electric Company
P. O. Box 982
El Paso, Texas 79960

Equal Opportunity Employer

EL PASO ELECTRIC COMPANY
P.O. Box 982
El Paso, Texas 79960





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Highlights 1979

	1979	1978	% Increase (Decrease)
Property and Plant:			
Total utility plant, year end	$2,735,073,000	$2,288,604,000	19.5
Capital expenditures	$ 468,116,000	$ 405,789,000	15.4
Sales and Customers:			
Total operating revenues	$ 664,423,000	$ 562,217,000	18.2
Total electric sales (mwh)	11,584,898	10,912,704	6.2
Electric customers, year end	401,983	378,553	6.2
Total gas sales (m therms)	467,088	449,451	3.9
Gas customers, year end	340,343	339,803	0.2
Income, Earnings, Dividends:			
Net income	$ 121,578,000	$ 106,759,000	13.9
Earnings for common stock	$ 99,696,000	$ 89,288,000	11.7
Average common shares outstanding	34,426,346	28,363,223	21.4
Earnings (based on average shares outstanding)	$ 2.90	$ 3.15	(7.9)
Dividends paid per share of common stock	$ 1.94	$ 1.73	12.1
Shareholders:			
Common	92,396	78,275	18.0
Preferred	7,049	7,158	(1.5)
Employees, year end:	5,263	4,951	6.3

Annual Report
This report is published to provide general information concerning the company and not in connection with any sale, offer for sale, or solicitation of an offer to buy, any securities.

Annual Meeting of Stockholders
All stockholders are invited to attend the company's sixtieth annual meeting. It will be held at 10 a.m. Thursday, April 24, in the Regency Ballroom of the Hyatt Regency Hotel, 122 North Second Street, Phoenix, Arizona.

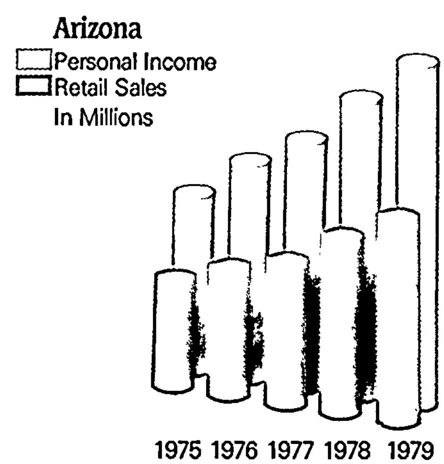
Our Cover:

The Arizona sky is ablaze with the sun, the ultimate energy source APS is working to harness for the future.

But while the search for new energy alternatives goes on, Arizona's energy needs continue to grow, reminding us of our more immediate task. And most of Arizona's energy needs—for the '80s—must be met with conventional sources.

These energy needs are growing at a time when energy issues have become the focal point of public debate and soaring inflation is pushing construction and operating costs higher and higher.

The planning, the people, the programs geared to meet these challenges as we begin a new decade are featured in your 1979 Annual Report.



Arizona Public Service Company, 411 North Central Avenue, Phoenix, Arizona