



140 BROADWAY NEW YORK, NY 10005

RAYMOND E. MOORE, CFA
(212) 320-3065

Trading (212) 320-3001

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ray.moore@shieldsandco.com

Prior Report July 3, 2007 -\$43 – Buy

Rating: Reduced from Buy to Hold

**Dominion Resources
(NYSE-D)**

It's VEPCO

Intraday	3/27					
D	31					
52-week range	48-27					
Book Value (12/31/08)	18.50	167.7%	P/B	Price	Ytd	12-Mos
Reported - Continuing	EPS*	P/E		Performance	3/27	
2005	2.26	13.7		Dominion	31	(13) (24)
2006	2.53	12.3		Phil. El. Index	350	(12) (31)
2007	2.56	12.1		Dow Industrials	7,763	(12) (37)
2008	3.16	9.8		Coverage		
2009 Estimate	3.20	9.7		Analyst Total	19	
2010 Estimate	3.30	9.4		Buy	5	26%
2011 Estimate	3.50	8.9		Shares (mil.)	577	
Dividend	1.75	5.6%	Yield	Market Val. -\$bil.	18	

* GAAP per share earnings: \$3.16 – 2008, \$3.88 – 2007, \$1.96 – 2006, \$1.50 – 2005.

Overview

Soon after Tom Farrell was elected Chief Executive Officer, effective January 2006, he along with the Board of Directors determined that Dominion Resources' profile was too risky relative to its shareholder base. Exploration & Production was profitable, albeit benefiting from surging energy prices, but over the long term, capital demands were huge, the business cyclical and competitors had equal or better expertise. E&P was sold, except for the Appalachia properties, in 2007 for \$9.5 billion with the proceeds used to retire debt, buy back common stock and hopefully leave a business mix more suited for the conservative utility investor.

In 2008, Dominion reported operating earnings before unallocated interest expense (\$0.41 a share) of \$3.57 a share. We estimate that \$1.95 a share (includes liquids of \$0.13 a share), or 55% of the total, was mostly regulated, \$1.30 a share (36%) merchant generation, and \$0.32 a share (9%) E&P-other. Investors remain lukewarm as to Dominion's prospects. According to Bloomberg Financial Service, Dominion has 19 active recommendations 5 buys, 2 sells, and 12 holds. We suspect the primary concern is Dominion's earnings exposure to energy prices at merchant generation.

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See page 9 of report for Analyst's Certification, pages 9-10 for Important Disclosures and page 10 for Other Disclosures and Disclaimers

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Guidance for 2010 of \$3.33-\$3.50 a share is based on natural gas prices for the un-hedged output of \$6.75-\$7.25 per mcf with each \$1.00 per mcf change equal to \$0.16 a share in earnings. Current natural gas prices in the \$3.75 per mcf area and 2010 futures in a range of \$5.00-\$6.00 per mcf, if unchanged, could reduce guidance to \$3.15-\$3.30 a share in 2010. Reductions in forecasts, even if anticipated, generally reduce stock prices.

Farrell's strategy for lowering risk remains unchanged, the key being the plain old utilities business. Virginia Electric and Power Company (VEPCO) encompasses regulated electric transmission and distribution (T&D), generation, and retail operations. VEPCO earned \$1.46 a share (\$847 million) and a 14.3% return on an average common equity of \$5,908 million. The company's \$7.5 billion construction program through the 2011 period would raise capitalization from \$12.5 billion in 2008 to \$16.3 billion in 2011. If VEPCO were to maintain a 14.3% return on average common equity, earnings would rise \$0.45 a share to \$1.90 a share in 2011. Dominion's 2011 earnings off a \$3.16 a share base in 2008 would increase to \$3.60 a share. Even if VEPCO's earned return on average common declines 100 basis points, earnings would increase \$0.30 a share to \$3.45 a share in 2011.

Dominion Resources' price performance has been mediocre, slightly underperforming the Philadelphia 22 Electric Stock Index and the SPDR year to date, 3-months and 6-months trailing. At \$31 a share, the shares trade at 9.7 times and 9.4 times estimated 2009 and 2010 earnings of \$3.20 and \$3.30 a share, respectively. The current dividend of \$1.75 a share represents a 55% payout and provides a 5.6% yield versus an average yield of 4.6% for its peers. The price/earnings ratio represents a 10-13% discount.

Investors' immediate concerns are the direction of energy prices and, later in 2009, the rate decision on the soon to be filed rate case. Significant cutback in guidance, beyond the \$0.16 a share benchmark, and a poor rate case could drop the stock to the \$27 a share area. On the upside, increase gas prices and a favorable rate case could raise the price to \$39 a share. The most significant development will be the outcome of the rate case and its implication for both earnings growth and the predictability of that growth.

For now we are going to the sidelines by lowering our rating from buy to hold, hopefully with an opportunity to raise our recommendation following any reduction in price via earnings cutbacks.

Table 1
Major Indices
Comparative Performance

Column	(1)	(2)	(3)	(4)	(5)	(6)
		Price				
		3/27 Intraday	YTD %	3-mos %	6-mos %	1-yr %
S&P 500	SPX	816	(10)	(6)	(33)	(38)
Phila. Index	UTY	350	(12)	(9)	(24)	(31)
SPDR	XLU	26	(11)	(9)	(26)	(32)
Dow Ind.	INDU	7,766	(12)	(9)	(30)	(37)
Dominion	D	31	(13)	(11)	(28)	(24)

Earnings Profile

In 2008, Dominion Resources reported ongoing operating earnings of \$3.16 a share (GAAP-\$3.16 a share), 23% higher than the \$2.56 a share (GAAP-\$3.88 a share) in 2007, and exceeding guidance of \$3.10-\$3.15 a share by a penny. Per share earnings benefited from an 11% reduction in shares outstanding from 655 million to 581 million, strong performances in generation and energy which more than offset increases in corporate and other. Generation operating earnings increased 83% from \$1.15 a share (\$756 million) to \$2.11 a share (\$1,227 million). Energy earnings grew 37% from \$0.59 a share (\$387 million) to \$0.81 a share (\$468 million). Virginia Power recorded a 3% gain from \$0.63 a share (\$415 million) to \$0.65 a share (\$380 million).

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Management issued 2009/10 guidance of \$3.20-\$3.30 a share (up 1%-4%) and \$3.33-\$3.50 a share (up 3%-8%), respectively. The forecast incorporates natural gas prices of \$6.25 per mcf in 2009 and a \$6.75-\$7.25 per mcf range for 2010. Each \$1.00 per mcf change in natural gas would change 2009 earnings by \$0.03 a share and 2010 by \$0.16 a share. Today natural gas prices are in the \$3.75 per mcf area. Current 2010 futures quotes are in the \$5.00-\$6.00 per mcf area, indicating that guidance for 2010 could be cut to \$3.15-\$3.30 a share, should prices remain unchanged. Management's long-term target is to grow earnings 6% annually.

Table 2 lists Dominion's earnings per share by business for 2008/07 and our estimates for 2009. Generation earnings are forecast at \$2.15 a share, Energy-\$0.80 a share, and Virginia Power-\$0.70 a share.

Table 2
Earnings per Share Profile

Segment	2009E			2008			2007		
	\$-Mil.	EPS	% Tot.	\$-Mil.	EPS	% Tot.	\$-Mil.	EPS	% Tot.
Generation	1,271	2.15	67	1,227	2.11	67	756	1.15	45
Energy	474	0.80	25	468	0.81	25	387	0.59	23
Va. Power	403	0.70	22	380	0.65	21	415	0.63	25
Primary	2,147	3.64	113	2,075	3.57	113	1,558	2.38	93
Corp. & Other	(250)	(0.42)	(13)	(241)	(0.41)	(13)	120	0.18	7
Consolidated	1,897	3.22	100	1,834	3.16	100	1,678	2.56	100
Shares-Mil		592			581			655	

Source: Company Year-End Release – Shields Estimates
Numbers may not add due to rounding

Generation

Generation capacity totals 27,090 megawatts, including 18,070 megawatts (67%) regulated and 9,020 megawatts (33%) merchant. Utility profits are a product of return on rate base. Merchant output is non-regulated and sold competitively in NEPOOL (76%) and PJM (24%). Generation combined EBIT was \$2,155 million in 2008 and derived 50/50 between utility (\$1,081 million) and merchant (\$1,074 million) before intercompany adjustments.

Utility: Utility generation profits decline in 2009 with increased refueling outages, higher non-outage O&M, increased depreciation rates and the need for rate relief. EBIT according to management will range from a negative \$69 million change to a modest \$11 million gain. Earnings in 2009 after allocation of interest expense (our estimate) and a 38% corporate tax rate decline to \$0.70-\$0.78 a share, versus \$0.81 a share in 2008.

Merchant: Sales in NEPOOL are projected to rise 12% in 2009 with 92% of the output hedged at \$79.89 a megawatt-hour. EBIT guidance forecasts increases of \$160-\$235 million in 2009. Earnings after allocated interest and income taxes could range from \$1.40-\$1.48 a share, up 8%-14% from 2008 earnings of \$1.30 a share. Merchant exposure to energy prices in 2010 is significant. Based on management comments, the earnings sensitivity to \$1.00 per mcf off of a \$6.75-\$7.25 per mcf range would change consolidated corporate earnings by \$0.16 a share.

Consolidated Generation: Combined 2009 results are expected to fall in a range of \$2.10-\$2.20 a share, versus \$2.11 a share in 2009. At current gas prices, profits could drop to the \$1.95-\$2.05 a share range.

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Table 3
Generation
Earnings & EBIT Guidance
2009-2008

Column	(1)	(2)	(3)
	2008	2009 Range	
Generation	\$-Mil.	\$-Mil.	\$-Mil.
Utility			
EBIT	1,081		
Weather		25	25
Revenues/other margins		80	115
Planned Outages		(53)	(44)
Non-outage O&M		(42)	(29)
DD&A		(44)	(36)
Other		(35)	(20)
Intercompany-other	(189)		
Cumulative Change		(69)	11
Adjusted EBIT	887	(69)	11
Cumulative EBIT	892	823	903
EBIT- PS	1.54	1.39	1.53
Interest Allocated	157	157	157
Pretax	735	666	746
Earnings Net @38%	471	413	463
Utility Per Share	0.81	0.70	0.78
% Change		(14)	(4)
Merchant			
EBIT	1,074		
Contracted Plants EBITDA		57	67
Non Contracted NEPOOL EBITDA		185	215
Non Cont. PJM EBITDA		(15)	0
DD&A		(47)	(37)
Other		(20)	(10)
Intercompany other	187		
Cumulative Change		160	235
Cumulative EBIT	1,261	1,421	1,496
EBIT-PS	2.17	2.40	2.53
Interest Allocated	81	81	81
Pretax	1,180	1,340	1,415
Earnings Net @38%	755	831	877
Merchant Per Share	1.30	1.40	1.48
% Change		8%	14%
Consolidated Per Share	2.11	2.10	2.26
% Change		0%	7%

Source: Management Guidance for Year-End 2009, Earnings Guidance Kit, page 11,
Shields Estimates

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Energy

Energy businesses include 1) regulated natural gas distribution, 2) transmission, 3) storage, 4) aggregation, and 5) exploration and production (E&P). Energy earned \$0.81 a share (\$468 million) in 2008 on EBIT of \$884 million. In 2009, earnings are expected in an \$0.80-\$0.89 a share range.

Distribution: East Ohio Gas is a regulated gas distribution system subject to the jurisdiction of the Ohio Public Utilities Commission. In October 2008, East Ohio was granted a \$40 million increase on a \$1,067 million rate base. The decision provided for an effective 11.4% return on a common equity component of 45%. Earnings power works out to \$66 million, or \$0.11 a share. Guidance in Table 4, suggests an earnings level in 2008 of \$0.13 a share and an increase to the \$0.15-\$0.17 area in 2009.

Table 4
Distribution – East Ohio Gas
Earnings & EBIT Guidance

Column	(1)	(2)	(3)
	2008	2009 Range	
Distribution	\$-Mil.	\$-Mil.	\$-Mil.
EBIT	154		
Normalized Weather		(9)	(9)
Rate Design		29	40
Other		5	7
Total		25	38
Cumulative EBIT		179	192
EBIT-PS	0.27	0.30	0.32
Interest Allocated	35	35	35
Pretax – mil.	119	144	157
Pretax - PS	0.20	0.24	0.27
Earnings @37.5% rate	0.13	0.15	0.17

Source: Company Year-end Release-Earnings Guidance Kit, page 10
Numbers may not add due to rounding

Transmission & Storage: The company's \$1.9 billion natural gas transmission system is FERC-regulated and, based on its last rate proceeding, was authorized a pretax return on rate base of 13.7%. We estimate regulated transmission earnings (40% common equity and a 14% return) at \$0.18 a share (\$106 million). Transmission earnings are boosted by selling non-regulated natural gas liquids. Liquid sales totaled \$227 million in 2008 less \$106 million shrinkage for a net \$121 million addition to pretax margins. At a 38% tax rate, liquids would have contributed \$75 million (\$0.13 a share) in 2008. Combined transmission and liquids businesses' return on common in 2008 is estimated at 18% and bottom-line earnings at \$0.31 a share.

Cove Point is an LNG facility located at Cove Point, Maryland. The company recently completed a \$900 million expansion, raising its investment to \$1.3 billion. Deliveries are scheduled to begin April 1, 2009. We estimate Cove Point earnings at \$0.05 a share in 2008.

In 2009, lower liquids margins are expected to be offset by increased volumes at Cove Point. EBIT is forecast at \$480-\$510 million, versus \$428 million in 2008. Earnings net of allocated interest and income taxes could increase from \$0.36 a share in 2008 to \$0.41-\$0.44 a share in 2009.

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Table 5
Transmission & Storage
EBIT Guidance

Column	(1)	(2)	(3)
	2008	2009 Range	
Transmission & Storage	\$-Mil.	\$-Mil.	\$-Mil.
EBIT	428		
Transmission & Storage - Rev.		175	180
Byproducts Extraction		(72)	(58)
Other		(51)	(40)
Total		52	82
Cumulative EBIT	428	480	510
EBIT – PS	0.74	0.81	0.86
Interest Allocated	89	89	89
Pretax - mil.	339	391	421
Pretax- PS	0.57	0.66	0.71
Earnings @37.5%	0.36	0.41	0.44

Source: Company Year-End Release, Shields Estimates, Earnings Guidance Kit, page 10
Numbers may not add due to rounding

Exploration & Production: E&P is income derived on the Appalachian properties retained after the \$9.5 billion sale of Dominion's other oil & gas properties in 2007. Pretax Appalachia margins in 2008 were \$300 million with production of 57.6 bcfe, and sales margin of \$5.20 per mcf. Reduced sales margins (\$4.66 per mcf) and lower volumes (45 bcfe) should reduce pretax sales margins by \$90 million in 2009. Guidance in Table 6 has earnings declining from \$0.25 a share to \$0.14-\$0.17 a share in 2009.

Table 6
Exploration & Production
EBIT Guidance

Column	(1)	(2)	(3)
	2008	2009 Range	
E&P	\$-Mil.	\$-Mil.	\$-Mil.
EBIT	252		
Sales Margins		(77)	(57)
Other		(26)	(22)
Total		(103)	(79)
Cumulative EBIT	252	149	173
EBIT – PS	0.43	0.25	0.29
Interest Allocated	12	12	12
Pretax – mil.	240	137	161
Pretax – PS	0.41	0.23	0.27
Earnings @ 37.5%	0.25	0.14	0.17

Source: Company Year-End Earnings Guidance Kit, pages 10 & 16, Shields estimates
Numbers may not add due to rounding

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Services: Producer Services is an aggregator for smaller companies in the Appalachia region. Earnings are expected to average \$30-\$40 million annually (\$0.06 a share).

**Table 7
Services & Other
EBIT Guidance**

Column	(1)	(2)	(3)
	2008	2009 Range	
Producer	\$-Mil.	\$-Mil.	\$-Mil.
Producer EBIT	50		
Gross Margins		11	15
Cumulative	50	61	65
Pretax - PS	0.09	0.10	0.11
Interest Allocated	0	0	0
Pretax	50	61	65
Pretax - EBIT	0.09	0.10	0.11
Earnings 37.5%	0.05	0.06	0.07
Other EBIT		24	24
Other Pretax Per Share		0.04	0.04
Earnings @37.5%	0.02	0.03	0.03
Producer & Other @37.5%	0.07	0.10	0.11

Source: Company Year-End Release, Shields Estimates, Earnings Guidance Kit, page 10
Numbers may not add due to rounding

Virginia Power

Virginia Electric and Power (VEPCO) is the consolidated regulated electric transmission and distribution (T&D), generation and non-regulated retail operations. In 2008, VEPCO earnings of \$847 million (\$1.46 a share) represented a 14.3% return on average common equity of \$5,908 million.

Management's goal is simple: earn a steady-to-rising return on a growing rate base. According to the VEPCO 10K, construction expenditures are budgeted at \$7.5 billion over the 2009-11 periods: 2009 - \$2.7 billion, 2010 - \$2.3 billion, 2011 - \$2.5 billion. Capitalization stood at \$12.5 billion at 2008 year-end of which about 80%, or \$10.0 billion, is subject to the jurisdiction of the Virginia Corporation (VCC). Capitalization (a proxy for earnings power) should increase 11% in 2009 to \$13.9 billion, 8% in 2010 to \$15.0 billion, and 9% in 2011 to \$16.3 billion. If VEPCO were to maintain its return over the 2009-11 period, earnings would approximate \$1.60 a share in 2009, \$1.75 a share in 2010 and \$1.90 a share in 2011.

Management will file for rate relief in Virginia on April 1, 2009. Excluding a decision or settlement, the rates will be collected subject to refund effective September 1, 2009. Rate base will include known expansions for the period the rates are in effect, thus matching revenues with investment. Also the company will be allowed premium returns on a \$1.0 billion Virginia City Hybrid Energy Center by the Virginia legislation, and on two electric transmission lines by FERC. Our forecast assumes a jurisdictional rate base at 80% of 2009 VEPCO capitalization, or \$11,200 million, and a 50% common equity component of \$5,500 million. We estimate VEPCO consolidated earnings, assuming an earned return on average common equity of 13.3%, of \$1.50 a share (3%) in 2009, \$1.63 a share (9%) in 2010 and \$1.75 a share (8%) in 2011.

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Virginia Power, representing regulated electric T&D and non-regulated retail, reported \$0.65 a share in 2008. EBIT guidance in Table 8 is a range of \$687-\$712 million, up from \$634 million in 2008. The EBIT forecast incorporates kilowatt hour sales growth of 1.5% and an unspecified rate increase effective September 1, 2009. Earnings in 2009 are estimated at \$0.70-\$0.73 a share, versus \$0.65 a share in 2008.

Table 8
Virginia Power
Earnings & EBIT Guidance

Column	(1)	(2)	(3)
	2008	2009 Range	
Virginia Power	\$-Mil.	\$-Mil.	\$-Mil.
Distribution EBIT	495		
Transmission EBIT	139		
Total	634		
Weather		14	14
Revenues & other margins		60	65
DD&A		(18)	(13)
Storm Damage Rest.		18	28
Other		(21)	(16)
Total		53	78
Total EBIT	634	687	712
Interest (83%)	130	130	130
Pretax	504	557	582
Pretax PS	0.87	0.94	0.98
Earnings Net @38%	0.54	0.58	0.61
Retail EBIT	134		
Margins		0	5
Cumulative EBIT		134	139
Interest (27%)	27	27	27
Pretax	107	107	112
Pretax PS	0.18	0.18	0.19
Earnings Net @38%	0.11	0.11	0.12
Virginia Power EPS	0.65	0.70	0.73

Year-End Earnings Release, Earnings Guidance Kit, page 9, Shield Estimates
Numbers may not add due to rounding

Analyst's Certification

I Raymond E. Moore certify that the views expressed in this research report accurately reflect my personal views about the subject companies and their securities. I also certify that I have not been and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendations in this report. Other Dominion Resources reports issued by me are: 11/16/06 (\$80) – Buy – Target Price \$100; 9/26/06 (\$77) – Hold; 4/19/06 (\$73) – Hold; 3/12/04 (\$63) – Upgrade to Hold; 1/23/04 (\$62) – Under Perform; 12/27/02 (\$54) – Under Perform; 7/3/07 (\$43.5) – Buy.

Important Disclosures

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Buy Total return is expected to exceed significantly the average total return of the analyst's industry coverage universe over the next 12 months.

Market Perform & Hold Total return is expected to equal the average total return of the analyst's industry coverage universe over the next 12 months.

Sell Total return is expected to significantly under perform (15% plus) the total return of the industry coverage universe over the next 12 months.

Analyst's Ratings Distribution

		% Investment Banking
Buy	11%	0%
Hold	89%	0%
Sell	0%	0%

The principal risks to the achievement of our price targets include general market trends, disappointing earnings and lower energy prices and adverse regulatory developments

Our target prices are based on projected earnings for the following calendar year, and an assumed price/earnings ratio in line with the company's historical valuation or those of other companies with similar businesses and prospects.



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