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Initiating Coverage: BUY

Ameren Corporation
(NYSE-AEE)

Ameren	6/20						
Price	49						
52-week range	55-48				Price	Y-t-d	12 Mos.
Book Value (12/31/06)	31.86	153%	P/b		Performance	6/20	%
Reported Ongoing					Ameren	49	(9)
2004	2.84	17.2			Phil. Electric Index	520	5
2005	3.02	16.1	P/e		Dow Industrials	13,489	8
2006	2.66	18.3			Coverage		
2007 Estimate	3.30	14.8			Analyst Total	13	
2008 Estimate	3.45	14.1			Buys	3	
Dividend Per Share	2.54	5.2%	Yield		Shares (millions)	207	
					Market Value (\$Bil.)	10	

Summary and Recommendation

Ameren's price performance has been awful. Year-to-date its price dropped 9% versus gains of 5% and 8%, respectively, for the Philadelphia Electric Stock Index and the Dow Industrials. For the trailing 12 months, Ameren's price is down 3% compared to a 21% increase by the Philadelphia Electric Index and 22% for the Dow. Its price earnings ratios of 14.8 times and 14.1 times for 2007 and 2008, respectively, represent discounts of 11% and 5% to the average electric while the \$2.54 a share dividend provides a 5.2% yield versus the average 3.1%.

Ameren's ills stem from the expiration of the rate freeze in Illinois (representing 36% of consolidated 2006 earnings) and consumer and political reaction to what would have raised average residential rates 40% to 55%. The Illinois Legislature threatened to freeze rates at 2006 levels through 2010; an action, if upheld by the courts, would bankrupt the Illinois utilities. Rating agencies reacted by downgrading Ameren's debt. But resolution seems in the offing. The Legislature (which extended its session), Governor Blagojevich, and the Citizens Utility Board (CUB) are meeting with managements, and participants have indicated that settlement is likely. Although not a drop-dead date, the hope is to reach an agreement by July 1, 2007.

Exelon (EXC-Hold) and Ameren had offered relief of \$500 million (Ameren \$200 million - Exelon \$300 million) through 2010 and at least one representative countered with a \$1.3 billion proposal. We assume the parties decide on a \$1.0 billion number over a four year period and that Ameren's share is \$400 million. Earnings would be reduced by \$0.30 a share annually to \$3.30 a share in 2007 and \$3.45 a share in 2008. A less risky Ameren could trade in the \$60 a share area (plus 22%) and continue to provide an above-average 4.0% yield.

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If the parties fail to reach an acceptable compromise, it would be up to the courts, something few are willing to risk since it would create an environment where long-term decision making becomes impossible. Ameren shareholders would have to rely on Missouri operations to support dividends since insolvent Illinois utilities couldn't up-stream dividends to the parent. Missouri earnings are estimated in the \$1.70-\$1.75 a share area. If the Board were to adopt a \$1.50 a share dividend, yield support in the 3.5% range (industry average 3.1%) works out to a price in the \$43-\$45 area (minus 12%).

According to Bloomberg Financial Service, Ameren has 13 active recommendations including 3 buys and 10 holds. Its shareholder profile is conservative: Franklin Resources (15.2 million shares), Capital Research (14.5 million), Lord Abbett (10.3 million), Barclays Global (7.0 million) and Bank of America (6.7 million).

Earnings Profile

Ameren earnings were \$2.66 a share in 2006 versus \$3.02 a share in 2005 and \$2.84 a share in 2004. Normalized profits, excluding gains on asset sales and one-time items, were \$3.15 a share in 2006 versus \$3.06 a share in 2005.

By segment, Missouri regulated business earned \$1.30 a share (\$267 million) and accounted for 49% of consolidated results. Illinois regulated profits were \$0.56 a share (\$115 million - 21%), and non-rate regulated generation \$0.67 a share (\$138 million - 25%). A fourth category, "other," is a catchall containing non-allocated costs, income from tax incentive investments, gains from the sale of leveraged leases, etc. Other earned \$0.13 a share (\$27 million), but is not expected to contribute to future results.

Table 1
Business Segment Earnings
2006

	2006		
	\$-Mil.	Per Share	% Total
Regulated			
Missouri	267	1.30	49
Illinois	115	0.56	21
Total Regulated	382	1.86	70
Non-rate-Regulated			
Missouri*	54	0.26	10
Illinois*	84	0.41	15
Total Non-rate Regulated	138	0.67	25
Other	27	0.13	5
Consolidated	547	2.66	100

*Shields' estimate of profit allocation between states

Guidance

Earnings guidance is \$3.15 to \$3.60 a share for 2007, with sell-side consensus at the high end (\$3.54 a share). The low-end forecast was issued in February among concerns over the yet to be released Missouri rate order in May and we suspect legal angst pending resolution of the fuel procurement debate.

Estimates of non-regulated rate earnings are a matter of filling in the blanks. Missouri regulated guidance is \$305 million, Illinois regulated - \$115 million and "Other" - negative \$5 million. The remainder is non-rate regulated earnings. Our input assumes Missouri non-regulated earnings (representing its 40% ownership in Electric Energy Inc.) remain at \$54 million. All increases in non-rate regulated earnings stem from re-pricing in Illinois.

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At \$3.15 a share, non-rate regulated earnings rise 71% to \$1.14 a share (\$237 million). The earnings increase of \$99 million represents re-pricing revenues of \$160 million. At \$3.60 a share, non-regulated earnings rise to \$1.59 a share (\$330 million) and re-pricing revenues to \$315 million.

Table 2
Segment Profits Based on Guidance

Column	(1)	(2)	(3)	(4)	(5)	(6)
	3.15			3.60		
Regulated	\$-Mil.	Per Shr.	% Total	\$-Mil.	Per Shr.	% Total
Missouri	305	1.47	47	305	1.47	41
Illinois	115	0.56	18	115	0.56	15
Total Regulated	420	2.03	64	420	2.03	56
Non-rate-Regulated						
Missouri*	54	0.26	8	54	0.26	7
Illinois*	183	0.88	28	276	1.33	37
Total Non-rate regulated	237	1.14	36	330	1.59	44
Other	(5)	(0.02)	(1)	(5)	(0.02)	(1)
Consolidated	652	3.15	100	745	3.60	100

*Shields' estimate of profit allocation

Illinois Power Procurement

Under Illinois legislation 1) generation was fully deregulated as of January 1, 2007 and 2) distribution purchased power expenses changed from cost of service based to competitive via an auction process, the first of which was held September 2006. According to Ameren's 2006 10K, residential rates in Illinois will rise by 40% to 55%, including 60% to 80% for heating customers. A 50% increase in rates, based on 2006 usage, would raise combined residential and commercial revenues of Central Illinois Public Service, Central Illinois Light and Illinois Power by \$814 million annually - \$420 million residential and \$394 million commercial.

Predictably, consumers and politicians rioted. Governor Blagojevich and the House support legislation freezing rates at 2006 levels through 2010. The legislative session has been extended pending resolution of the electric rates controversy (also approval of a state budget). Should compromise talks fail, Ameren and Exelon appear on strong legal ground but appeals take time, heighten uncertainty and an adverse ruling is always possible.

Ameren and Exelon have clearly stated that a rate freeze would bankrupt Illinois utilities. Instead the companies proposed relief of up to \$500 million (\$300 million Exelon - \$200 million Ameren) through 2010 and at least one legislator countered with a \$1.3 billion number. Conferences are underway and press comments have been positive, some speculating on a \$1 billion credit. With a \$1 billion credit spread over four years, Ameren's 40% share would reduce earnings \$100 million (\$0.30 a share) annually.

Failure to reach settlement would put the \$2.54 a share dividend in jeopardy. Already below investment grade bond ratings would be cut further and if distributors were unable to pay bills, non-rate regulated generating earnings would decline. Initial write-downs would include \$755 million in goodwill plus \$697 million of regulatory assets. Illinois Power and Central Illinois Light (Cilcorp goodwill applies to Central Illinois Light) retained earnings turn negative, eliminating either company's ability to up-stream dividends to the parent.

(Exelon, in anticipation of a goodwill write off, set up an "appropriated retained earnings" reserve at Commonwealth Edison.)

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Table 3
Write Off of Goodwill & Regulatory Assets
2006

Column	(1)	(2)	(3)	(4)	(5)
	Retained Earnings	Goodwill	2006 Regulatory Assets*	Write Off*	Balance
	\$ Mil.	\$ Mil.	\$ Mil.	\$ Mil.	\$ Mil.
Central Illinois Public Service	302		146	91	211
Central Illinois Light	99		75	47	53
Cilcorp	11	542	75	589	(578)
Illinois Power	101	213	401	462	(361)
Total	513	755	697	1,187	(674)
Per Share	2.44	3.60	3.32	5.65	(3.21)
Ameren Consolidated	2,024	830	1,431		837
Per Share	9.64	3.95	6.81	5.65	3.99

*Assumes 38% consolidated tax for Regulatory Assets

Illinois Cost of Capital Case

Ameren's Illinois utilities filed for a \$202 million rate increase effective January 2, 2007 coincident with the end of the rate freeze. Central Illinois Public Service's request was \$14 million, Central Illinois Light - \$43 million, and Illinois Power - \$145 million. In November, the ICC approved \$97 million, including a rate cut for Central Illinois Public Service of \$8 million and increases of \$21 million and \$84 million, respectively, for Central Illinois Light and Illinois Power. The return on common was 10%, but according to management, costs disallowances of \$50 million and regulatory lag will depress returns to less than half of allowed levels.

Table 4
Illinois Cost of Capital Rate Cases
November 2006

	Request \$-Mil	Decision \$-Mil
Central Illinois Public Service	14	(8)
Central Illinois Light	43	21
Illinois Power	145	84
Total	202	97

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Missouri Cost of Capital Rate Order – May 22, 2007

The company's original request on July 7, 2006 was a \$361 million electric rate increase. After negotiations with the staff and other interveners the request was pared to \$245 million. On May 22, 2007, the Missouri Public Service Commission (MPSC) approved a \$43 million increase based on a 7.9% return on a rate base of \$5,637 million and a 10.2% return on a \$2,925 million common equity. The bulk of the difference between the \$245 million requested and the \$43 million granted includes 1) lower allowed return on common from 12.0% to 10.2% - \$94 million, 2) reduction in depreciation rates assuming 20 year life extension at the Calloway nuclear plant - \$27 million, and 3) higher level of assumed off system sales - \$27 million.

Table 5
Missouri
Electric Rate Decision
May 22, 2007

Column	(1)	(2)	(3)	(4)
	\$ Mil.	Cost	% Total	Weighted Cost %
Long-Term Debt	2,552	5.5	45.3	2.5
Short-Term Debt	45	5.4	0.8	0.0
Preferred Stock	115	5.2	2.0	0.1
Common Equity	2,925	10.2	51.9	5.3
Total	5,637		100.0	7.9

Regulated earnings power in Missouri is \$1.47 a share (\$313 million) based on the 10.2% equity return, including electric of \$1.44 a share (\$298 million) and gas \$0.07 per share (\$15 million). Management guidance incorporates 2007 earnings of \$1.47 a share (\$305 million).

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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.

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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.

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Hold	80%	0%
Sell	0%	0%

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