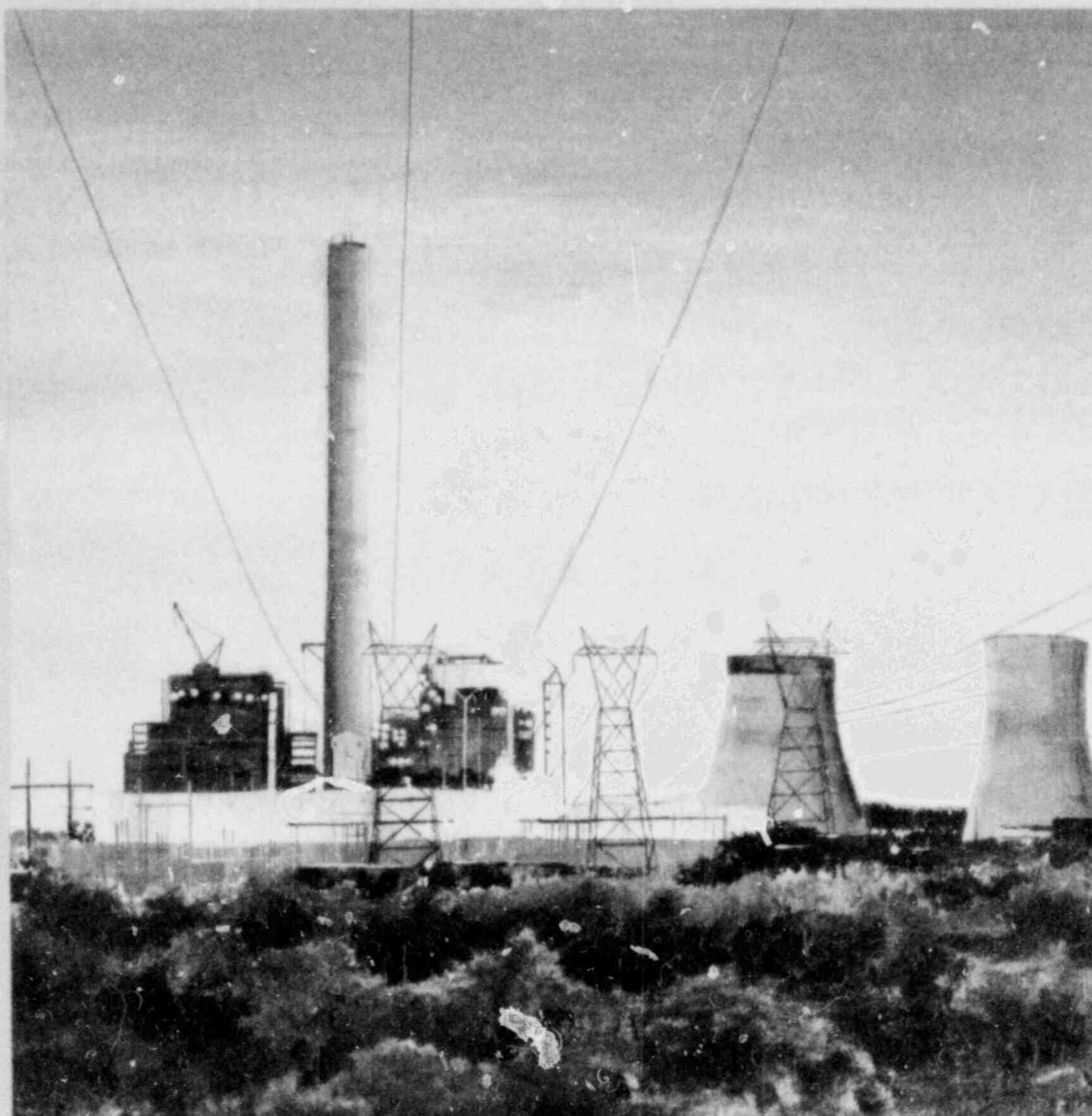
MIDDLE SOUTH UTILITIES, INC.

1980 ANNUAL REPORT



PERFORMANCE HIGHLIGHTS

	1980	1979	1978	Percent Change '80	Percent Change '79
Total Operating Revenues (millions)	**$2,342**	$1,823	$1,622	28.5	12.4
Total Operating Expenses (millions)	**$2,044**	$1,605	$1,394	27.4	15.1
Fuel, Purchased Power & Purchased Gas Costs (millions)	**$1,317**	$1,045	$ 826	26.0	26.5
Operating Income (millions)	**$ 298**	$ 218	$ 228	36.7	(4.4)
Net Income (millions)	**$ 196**	$ 182	$ 185	7.7	(1.6)
Allowance for Funds Used During Construction (millions)	**$ 240**	$ 213	$ 148	12.7	43.9
Rate of Return on Average Common Equity (percent)	**10.98%**	11.82%	14.19%		
Earnings Per Share (dollars)	**$ 2.01**	$ 2.13	$ 2.46	(5.6)	(13.4)
Dividends Paid per Share (dollars)	**$ 1.58**	$ 1.52	$ 1.44	3.9	5.6
Customers (Electric—Year-end)	**1,546,733**	1,520,142	1,489,188	1.7	2.1
Total Electric Energy Sales (billion kwh)	**55**	53	52	3.8	1.9
System Peak Load (kilowatts)	**11,769,000**	10,687,000	10,648,000	10.1	0.4
Gross Utility Plant at Year-end (billions)	**$ 7.9**	$ 7.0	$ 6.1	12.9	14.8
Construction Expenditures (millions)	**$ 910**	$1,025	$ 901	(11.2)	13.8
Common Stock (Number of shares, in thousands) Average	**97,469**	85,445	75,522	14.1	13.1
At year-end	**107,350**	90,433	76,098	18.7	18.8

ABBREVIATIONS: In this report, references to companies in the Middle South Utilities System are as follows:

MSU or the Company ...... Middle South Utilities, Inc.
MSS .... Middle South Services, Inc.
MSE .... Middle South Energy, Inc.
AP&L .... Arkansas Power & Light Company
Ark-Mo .... Arkansas-Missouri Power Company
LP&L .... Louisiana Power & Light Company
MP&L .... Mississippi Power & Light Company
NOPSI .... New Orleans Public Service Inc.
SFI .... System Fuels, Inc.
Associated .... Associated Natural Gas Company

My Fellow Stockholders:

In describing the 1980 results for our Middle South Utilities System, I think it would be fair to characterize the year as one of "turning the corner" toward greater financial vitality, more responsive regulatory treatment, and improved ability to serve the energy needs of the System's 1.5 million customers.

We made substantial progress toward our goal of diversifying the System's fuel base to lessen our dependence on fuel oil and natural gas as fuels for electric generation. This progress was marked by completion and commercial operation of our second nuclear-fueled generating unit and our first modern coal-fueled unit, both in Arkansas. These two units added 1,673 megawatts to the System's generating capacity and, at normal operating load factors, can displace 16 million barrels of very expensive fuel oil per year. As the System's remaining six generating units now under construction — three coal, three nuclear — are completed and go into commercial operation, the heavy construction financing load which the System has been carrying in recent years can be expected to bear fruit, with renewed financial vigor for the System, much-improved ability to serve our customers' electric energy requirements at the lowest practicable cost through displacement of ever-more-costly oil and gas, and adequate capacity for area growth.

Our consolidated net income, which dipped slightly from 1978 to 1979, increased almost eight percent in 1980. This improvement was mainly attributable to three factors: rate increases placed in effect during the year by several of the System operating companies, heavy electric energy requirements by our customers during a widespread, sustained record-setting period of hot weather last summer, and continued tight control of expenses.

As a necessary part of financing the System's essential construction program, the Company sold additional common stock through underwritten public offerings on two occasions in 1980. The higher average number of shares thus outstanding in 1980 caused earnings per share to decline from $2.13 per share in 1979 to $2.01. It is the considered judgment of your management team and board of directors that your long-run best interests, considering the tremendous changes which have occurred in world fuel markets in the last decade, demand that the System's coal and nuclear program be carried through to successful completion.

During 1980, construction expenditures totaled $910 million, compared to $1.025 billion in 1979. We expect that capital expenditures for construction for 1981 will be approximately $897 million.

The System's retail customers required five percent more electric energy in 1980 than in 1979, again heavily influenced by the extreme temperatures of the summer of 1980. Our forecasts, based on normal weather, indicate that customer requirements for electricity will grow at a slower rate in the 1980s than was experienced in the 1970s, but we believe that in our Middle South service area — in the Sunbelt, with the nation's only deep-water oil port soon to open, and many other industrial advantages — customer electric energy requirements will grow faster than those of the nation as a whole. Thus, our construction of new generating facilities is not only for the purpose of fuel diversification but also to ensure that the System will have the ability to meet those future needs when they arise.

The business in which you have invested is basically the serving of essential electric energy needs of the people and institutions of some 92,000 square miles. And to this we are deeply dedicated, but with the clear qualification that the System must be accorded the realistic opportunity to earn a fair return for our stockholders, to compensate you adequately for the use of your capital. To achieve this needed level of earnings, the System

CONTENTS

ABOUT THE COVER

The Middle South Utilities System's first modern coal-fueled electric generating plant, White Bluff, Unit 1, near Redfield, Arkansas, began commercial operation in August 1980.

operating companies have been diligent in seeking needed rate increases while striving to minimize operating expenses. As reported to you in last year's annual report, we began to see progress in the rate area in the second half of 1979, and this trend continued in 1980. Unquestionably one of the keys to sustained financial health for the electric utility industry is the overcoming of regulatory agencies' practice of treating investment capital as of no interest or benefit to customers until a project goes into commercial service. As an investor you certainly put your capital into the total Company and its programs for service to customers now and in the future; and you are entitled to a fair return from the business without having to try to trace the facilities where each dollar of your investment is actually spent. We believe that some progress is being made in getting regulators to recognize that if customers' needs (whether for added energy or to offset sky-rocketing oil costs) are served by construction of facilities, the customers' interest in the facilities does not come into existence only at the instant of initial commercial operation of the facility. All dollars of investment to support needed construction should be included in the base on which the business is permitted to earn when the investment is made; and extensive studies have shown that over the life of the facility, customers would actually pay less under such procedure. For a detailed discussion of the System's current rate situation, see page 7 of this annual report.

Last year, I reported to you on the electric utility industry's efforts to respond appropriately to the March 1979 accident at the Three Mile Island nuclear plant in Pennsylvania. Further progress was made in 1980 in the industry's substantial effort to apply the lessons learned at Three Mile Island. One significant milestone was the establishment in September 1980 of Nuclear Electric Insurance Limited (NEIL), a mutual insurance organization funded by the industry. Coverage by NEIL will greatly alleviate the financial burden placed upon an insured utility experiencing an extended outage of a nuclear generating plant due to an accident by paying a portion of the replacement power costs incurred. Middle South has secured this added insurance coverage for its nuclear units.

Probably one of the most important accomplishments of 1980 was the institution of the Significant Event Evaluation and Information Network (SEE-IN). By means of this program every non-normal event at any U.S. nuclear generating plant is carefully analyzed by the Nuclear Safety Analysis Center and the Institute of Nuclear Power Operations for its generic significance. Where the analysis indicates the need for corrective action, this is immediately communicated to every nuclear plant in a manner calculated to secure such action. I do not believe it is overstating the case to say that if SEE-IN had been in operation at the time of a precursor event at another nuclear plant similar to the happening at Three Mile Island, most of us and certainly the national public would never have heard of TMI.

The continued work of the Nuclear Safety Analysis Center, the Institute of Nuclear Power Operations, the Committee for Energy Awareness, and NEIL has been important in the effort to restore the American public's confidence in nuclear power. Opinion polls indicate that the majority of Americans continue to recognize the importance of nuclear power and support its continued use, just as they did prior to the Three Mile Island accident.

We are encouraged by the nuclear positions which have been enunciated by the Reagan administration, and will cooperate fully in efforts to assure nuclear power's role in meeting America's energy goals.

During 1980, we inaugurated a new strategic planning process to formalize, coordinate, and bring into sharper focus the manner in which the System considers its future environment, weighs its alternatives, and plans appropriate actions in furtherance of its basic goals. We believe that this more structured strategic planning program will help us to cope well with the increasingly difficult economic, energy, and regulatory challenges of the future. See page 38 of this annual report for a list of the corporate objectives which form the basis of this strategic planning process.

The consolidation of operations of Arkansas Power & Light Company and Arkansas-Missouri Power Company became effective January 1, 1981. Ark-Mo is now a division of AP&L, and Associated Natural Gas Company, formerly an Ark-Mo subsidiary, is now a subsidiary of AP&L.

After almost 25 years with Middle South Utilities, Donald J. Winfield, senior vice president, who for many years was the chief financial officer for the System, will reach normal retirement on March 31, 1981. Following a successful career with a prominent investment counseling firm, he joined Middle South in 1956. Mr. Winfield has served Middle South with unusual skill and professionalism in its financial affairs. Inasmuch as his successor, Edwin Lupberger, is located in our New Orleans headquarters, the New York office is being closed.

As you were informed by letter in January 1981, a large portion of your 1980 dividends represented, for federal income tax purposes, a return of capital and, for that reason, were nontaxable as income. See page 39 of this report for more details concerning this determination.

Your board of directors, in declaring the dividend payable January 2, 1981, raised the quarterly dividend rate to 40½¢ per share. This is equal to an annual rate of $1.62. Since its formation, the Company has been able to increase the dividend every year except one, 1956.

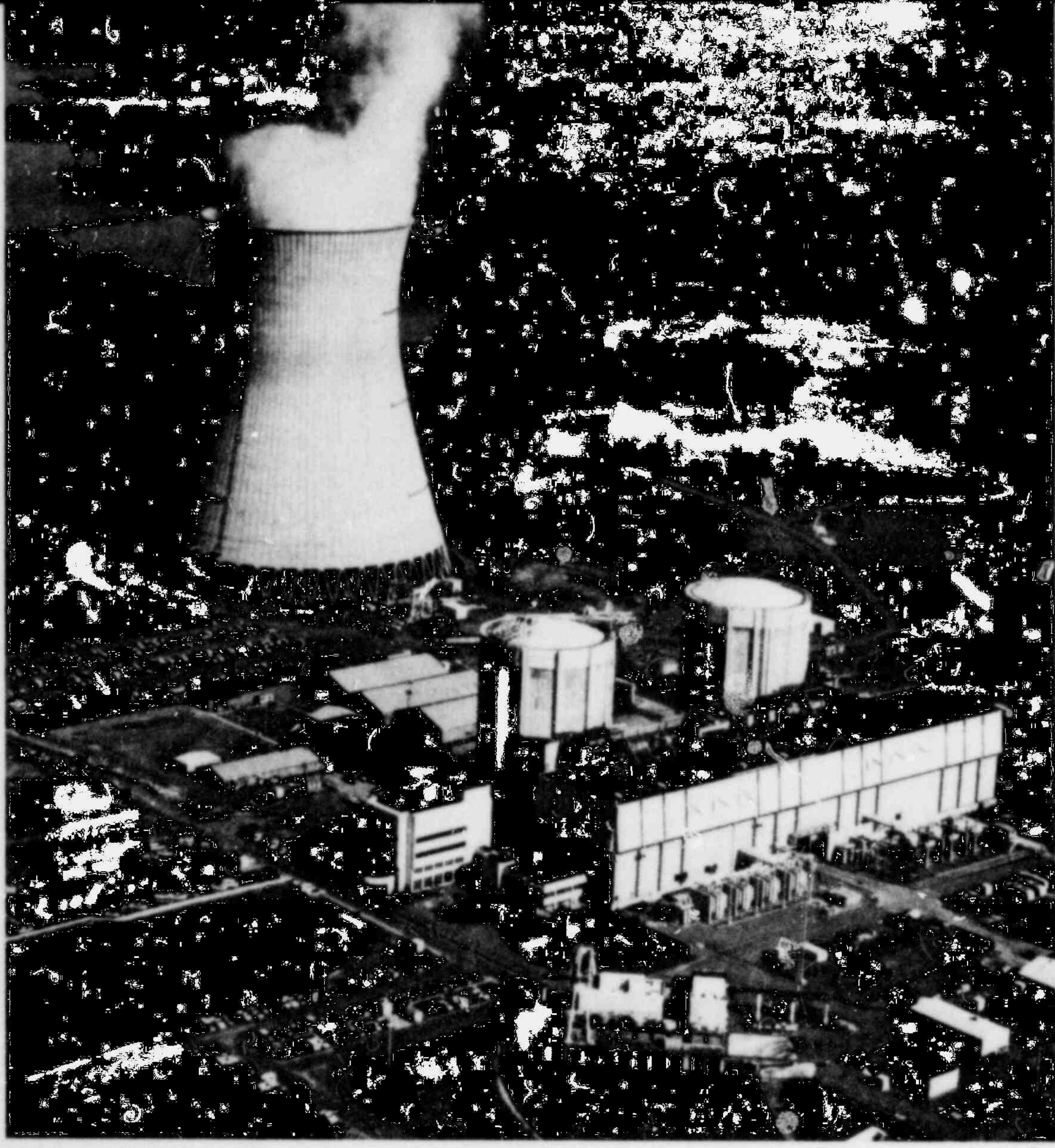
A new discount feature initiated at mid-year made the Company's Dividend Reinvestment and Stock Purchase Plan an even more attractive option. Beginning with the July 1, 1980, dividend payment, reinvested dividends were applied toward the purchase of Middle South common stock at a five-percent discount. Such purchases are made without brokerage fees or commissions. If you are not doing so already, and you would like to avail yourself of the savings and convenience of this plan, please write to Dan E. Stapp, secretary of the Company.

On behalf of the board of directors and my 12,000 fellow employees in the Middle South Utilities System, I thank you for your continued support of our efforts.

Sincerely,

F W Lewis

Floyd W. Lewis
Chairman & President



Aerial view of Arkansas Nuclear One, Units 1 and 2, near Russellville, Arkansas. Unit 1, the Middle South System's first nuclear-fueled electric generating plant, was placed in commercial service in 1974. Unit 2 began commercial operation in March 1980.

FINANCIAL REVIEW. Financially, 1980 was a year of building for a stronger future while continuing the Middle South Utilities System's large program of power plant construction. Maintaining this program of adding generating capacity has been difficult due to inflation, regulatory uncertainty and delay, and inadequate rate relief. The Company's financial position, as is the case for most of the companies of the electric utility industry, has been weakened because regulators have not allowed system operating companies to increase rates to pay for the substantial cost of funds associated with construction. As a result, cash generated from operations has been declining in recent years.

New rates placed in effect since December 1979 have been significant. The increases generally related to higher operating costs resulting from inflation and growth of the business. The costs of funds related to construction are not, for the most part, being recovered in current revenue. A key corporate objective is to gain regulatory acceptance of the need to provide current revenue to recover these costs of capital.

REVENUES. For 1980, the total operating revenues of the System reached $2.3 billion, 28.5 percent above those of 1979. Electric revenues increased also, rising 30.7 percent to $2.2 billion. The increases resulted from higher energy sales, particularly during the record-breaking hot summer, and from rate increases placed in effect by System operating companies. Another factor was recovery of the greatly increased costs of fuel (both fuel oil and natural gas) experienced in 1980.

Gas revenues for 1980, $117 million, represented a two-tenths of one percent increase over 1979. The increase is largely attributable

When unit coal trains from Wyoming arrive at the White Bluff plant site, special equipment unloads cars individually by turning them over and dumping the coal.

to recovery of higher costs for purchased gas.

NOPSI's transit revenues for the year were $44 million, an increase of 19.2 percent. Commencing in 1977, NOPSI has annually negotiated with the City of New Orleans a subsidy and indemnity agreement which assures that company of earning a specified rate of return on the transit rate base. NOPSI is working with city and state authorities toward the establishment of a regional transit authority and ultimate divestiture of transit operations. The New Orleans City Council in 1979 stated a policy objective of acquiring the transit system at some unspecified future date.

EXPENSES. Total operating expenses rose $440 million, or 27 percent, to $2 billion. As has been the case in almost every year since the oil embargo, increased costs for fuel, purchased power and purchased gas have been a major factor in the increases in operating expenses. The increase for 1980 was $272 million to a level of $1.3 billion. Of this increase in cost, approximately 90 percent is due to price increases, with the remainder being attributable to increased volumes purchased. Combined, these expense categories made up 64 percent of the System's total 1980 operating expenses.

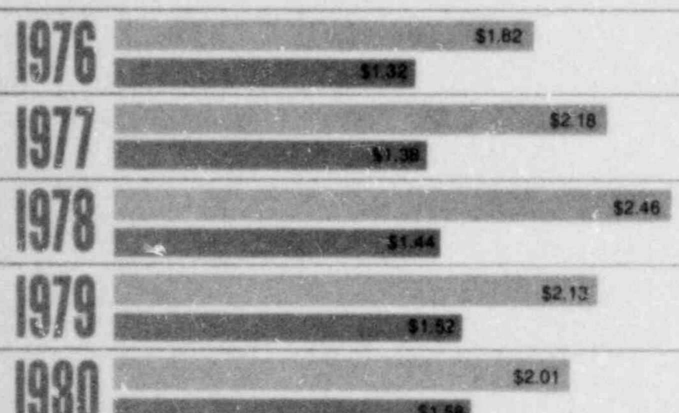
Other operating expenses, including taxes, continued to increase in response to inflationary pressures and the placing in service of two new generating units.

Costs of financing — interest charges and preferred dividend requirements — increased $122 million or 36 percent over 1979, reflecting the large amount of external financing required in 1979 and 1980 and the unprecedented high level of interest and dividend rates prevailing throughout these periods. The increased costs are for the most part related to our financing of construction projects — new capacity not yet placed in service.

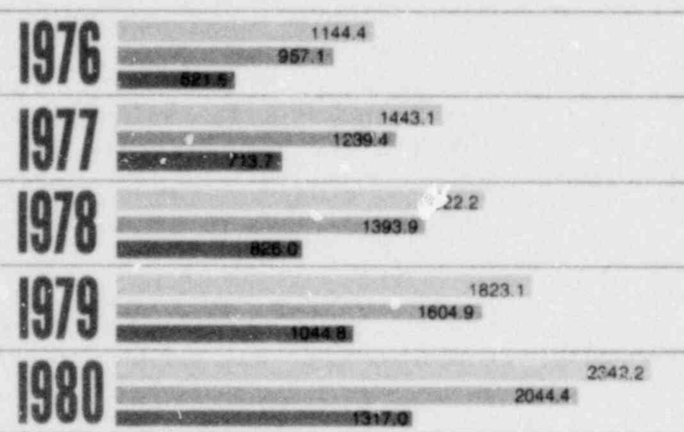
CONSOLIDATED NET INCOME, EARNINGS. Net income increased from $182 million in 1979 to $196 million in 1980. This 7.7-percent increase is primarily attributable to higher-than-normal summer energy sales in 1980 and new rates placed in effect by System operating companies during the second half of the year.

Earnings per share decreased from $2.13 in 1979 to $2.01 in 1980. There was a 14-percent greater average number of shares outstanding in 1980 than in 1979.

EARNINGS AND DIVIDENDS PAID
(Dollars per Share)
Earnings Dividends



REVENUES AND EXPENSES (Millions of Dollars)
Operating Revenues Operating Expenses
Fuel and Purchased Power Costs*



*Includes fuel for electric generation, purchased power and gas purchased for resale. (Included in operating expenses.)

Mechanized coal train unloading equipment is operated from this control booth overlooking the delivery point.

ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION (AFDC). As a general rule, the System's regulators have not allowed System operating companies to increase rates to recover current costs (interest and dividends) of funds raised to finance construction of projects not yet in service (construction work in progress). These costs of construction funds include interest on borrowed funds, dividends on preferred stock, and a reasonable return to the common stockholder (which includes common dividend requirements). However, these costs are expected to be recovered through revenue collected in the future (once the construction is placed in service). Therefore, the estimated amount of these costs is added to the value of the project under construction — an increase in asset value is recognized. *This increase in value of assets of the corporation is recognized in the income statement of the current year and has the effect of removing from the income statement the effect of the construction financing costs.* The amount is reported as Allowance for Funds Used During Construction in two parts: an amount representing costs of funds invested by common and preferred stockholders, and a second amount equivalent to the after-tax cost of borrowed funds. The total amounts included in net income in 1980, 1979, and 1978 were: $240 million, $213 million, and $148 million, respectively. While these credits to the income statement remove the effect of the costs of financing construction, they do not provide any cash to the business. The System has consistently and vigorously been asserting in regulatory proceedings that financing costs should be recovered in current revenue and not deferred to future years.

Until regulators allow recovery of substantial amounts of these costs of capital in current revenue, internal cash flow will be restricted and the System will continue to have to depend on new external financing for the construction program more heavily than it should, in the interest of both investors and customers.

1980 FINANCING. The System's construction program required the raising of substantial amounts of investment capital during the year 1980.

MSU had two common stock offerings during 1980. A sale in April of seven million shares, sold to underwriters through competitive bidding at $12.26 per share, for public resale at $12.65 per share, netted the Company $86 million. A second sale in October of eight million shares, again sold to underwriters through competitive bidding, netted proceeds of $94 million. The shares, sold for $11.75, were resold to the public at $12.13 per share. Proceeds from these two sales were used to retire outstanding bank debt.

Among MSU subsidiaries, AP&L raised the most capital in 1980 through sales of preferred stock and first mortgage bonds. The January 1980 sale of two million shares of $25

FINANCIAL REVIEW

The low-sulfur Wyoming coal, after being unloaded from the rail cars, is sent by a conveyor system either to storage for later use or to a pulverizer, where it is crushed to a powdery consistency and then blown into the boilers for combustion.

par value, 13.28-percent preferred stock brought proceeds of $50 million. In December, AP&L went to the financial market again — this time with the sale of 16 ⅛ percent, six-year first mortgage bonds. Proceeds from that sale totaled $70 million, bringing AP&L's average cost of money for new senior capital to 14.9 percent for 1980. In coordination with Pope and Jefferson counties in Arkansas, an additional $16.6 million of pollution control bonds were sold in December 1980.

LP&L also made two trips to financial markets in 1980, resulting in an average cost for new senior capital of some 16.0 percent. In November LP&L received $28 million from a sale of 1.2 million shares of $25 par value, 15.20-percent preferred stock. In December, LP&L raised $49 million from the sale of 15 ¾-percent eight-year first mortgage bonds.

NOPSI received $15 million through a sale in March of 150,000 shares of $100 par value, 15.44-percent preferred stock.

MSE received $98.5 million from the sale of 12½-percent, 20-year first mortgage bonds. These bonds were issued in January, April, and July in amounts of $15 million, $31.5 million, and $52 million, respectively.

Equity investments by the Company in the common stocks of AP&L, LP&L, and MSE totaled $157.9 million in 1980. Funds for these investments were raised through bank loans, which have been or will be repaid from proceeds of MSU common stock sales to the public through underwriters.

MSU successfully negotiated a $230 million revolving credit line with a group of

SELECTED FINANCIAL DATA

	1980	1979	1978	1977	1976
Net Operating Revenues*	$2,342,228	$1,823,059	$1,622,177	$1,443,057	$1,144,411
Net Income*	$ 195,907	$ 182,058	$ 185,438	$ 144,969	$ 106,047
Earnings Per Share	$2.01	$2.13	$2.46	$2.18	$1.82
Dividends Declared Per Share	$1.59	$1.535	$1.46	$1.395	$1.335
Total Assets*	$7,334,879	$6,503,068	$5,501,027	$4,736,707	$4,136,235
Long-Term Debt (excluding current maturities)*	$3,392,309	$3,017,816	$2,629,711	$2,175,471	$1,965,985
Preferred Stock with Sinking Fund*	$ 283,165	$ 193,507	$ 60,063	$ 60,063	$ 60,063

*(In Thousands)

money center and regional banks which will cover the Company's short-term needs through 1984. The line will contract as projected needs are reduced, dropping to 75 percent of the original amount in 1983 and 50 percent in 1984. The credit agreement became effective June 27, 1980.

1981 FINANCING. System construction expenditures for 1981 are estimated to be $897 million, excluding nuclear fuel costs. SFI expects to increase its investment in fuels-related programs other than nuclear by $8 million. Nuclear fuel costs in excess of those previously provided for in existing lease agreements are expected to be $107 million. Retirement of bonds approaching maturity and other capital requirements call for some $125 million, bringing to $1.137 billion the System's total capital needs anticipated for 1981.

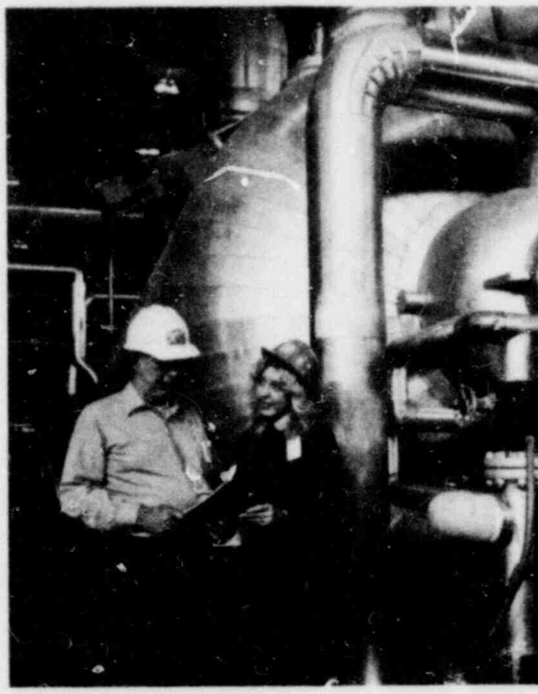
The System expects to raise approximately $837 million of the required funds from external sources, including the sale of first mortgage bonds and preferred stock, long- and short-term bank loans, sale and lease-back of properties, leasing of nuclear fuel, pollution control bond financing, and sale of MSU common stock.

The balance of projected capital requirements, an estimated $292 million, will be met by the System with internally generated funds.

The Company expects to raise approximately $206 million in 1981 through the issuance and sale of additional shares of common stock. A portion of these funds will be raised through an underwritten public offering tentatively set for late April 1981.

Total investments by MSU in the common stocks of System companies in 1981 are estimated at $123 million. Funds for these investments are expected to be raised through bank borrowing — repaid through the sale of additional shares of MSU common stock. The remaining proceeds from the sale of MSU common stock, approximately $83 million, will be used to reduce bank loans outstanding.

CAPITALIZATION. Capitalization ratios at year-end were as follows: long-term debt, 57.5 percent; preferred stock, 10.4 percent; and common equity, 32.1 percent. The capital structure reflects the weakened financial position of the Company, which has developed as our construction investment accelerated in recent years. Management recognizes the need to strenghten the ratios and is developing plans to increase the common equity portion of the ratio.



Construction engineers give Arkansas Nuclear One, Unit 2, a thorough checkout prior to its initial commercial operation in March 1980.

RATE ACTIVITIES. The financial condition of the Middle South System is closely related to the adequacy of rate relief received from the various regulatory bodies with jurisdiction over its operations. During 1980 all of the operating companies filed for rate increases. At year-end 1980, System companies had pending or on appeal electric and gas rate increase applications totaling approximately $465 million on an annual basis.

AP&L. On May 29, 1980, AP&L filed with the Arkansas Public Service Commission (APSC) a request for a two-step retail rate increase totaling some $130 million, with $86.7 million to be placed in effect immediately and the remainder to be placed in effect June 1, 1981. The first step, $86.7 million, was put in effect, subject to possible refund, on October 28. On November 26, AP&L and the APSC staff entered into a stipulation agreement whereby the staff recommended an increase of approximately $90 million and, in return, AP&L agreed not to contest certain staff adjustments which would have the effect of reducing AP&L's request to approximately $117 million, as opposed to the $130 million originally sought. Hearings have been concluded, and AP&L was awaiting a final order as this report went to press.

On August 28, 1980, AP&L asked the Federal Energy Regulatory Commission (FERC) for an increase of almost $10 million in its wholesale rates, pursuant to a pre-filing settlement agreement with AP&L's wholesale customers. AP&L began collecting the first phase of the increased rates, amounting

FINANCIAL REVIEW

Dispatchers who specialize in computerized power dispatch constantly monitor the System's energy load at the MSU System Operations Center in Pine Bluff, Arkansas. One of their jobs is to ensure that electricity is generated using the most economical facilities available.

to some $7 million on an annual basis, on November 2, 1980, subject to possible refund.

Ark-Mo, now a division of AP&L, filed with the APSC on July 23, 1980, for a retail increase of some $7.5 million. The full amount was placed in effect on December 21, 1980, subject to possible refund. Hearings had not begun when the year ended and Ark-Mo became a part of AP&L.

LP&L. On May 30, 1980, LP&L requested the Louisiana Public Service Commission (LPSC) to increase its retail rates by $203.6 million annually. On October 8, LP&L was allowed to place in effect on an interim basis an increase of $32.4 million, while the LPSC considers the original request. A decision of the LPSC is expected in May 1981.

LP&L also serves one ward of the City of New Orleans, where the New Orleans City Council holds regulatory authority. On July 3, 1980, LP&L asked the City Council for an increase of approximately $4.4 million per year in order to align its New Orleans rates with those being sought for customers outside the city. On October 24, LP&L asked for some $704,000 on an interim emergency basis. Hearings on the original $4.4 million request and the $704,000 interim filing had been held at year's end.

MP&L. A request for a $68.8-million annual increase in retail rates was filed by MP&L on May 28, 1980 with the Mississippi Public Service Commission (MPSC). MP&L placed the rates in effect, under bond and subject to possible refund, on July 1. On November 24, the MPSC rendered a decision granting MP&L a rate increase of $48.3 million per year. This decision has been appealed to the state courts by MP&L and by two intervenors in the case, the state attorney general's office and the Mississippi Legal Services Coalition. MP&L, in appealing, is asking for the full amount originally requested and is seeking inclusion in the rate base of Construction Work in Progress. Pending a final decision, the full amount of the rate increase originally sought will continue to be collected.

NOPSI. On April 14, 1980, NOPSI filed with the City Council of New Orleans a request for increases in its electric and gas rates totaling $32.5 million per year ($23.3 million for electric, $9.2 million for gas). At year's end, hearings in the case had been concluded, and NOPSI was awaiting the Council's decision.

COMMON STOCK DATA

	Quarter			
1980	**First**	**Second**	**Third**	**Fourth**
Price Range				
High	13 ⅛	14 ¼	13 ⅝	12 ⅞
Low	10 ¼	11	11 ½	10 ⅝
Dividend Declared	$0.395	$0.395	$0.395	$0.405
1979				
Price Range				
High	16 ¼	15 ⅜	16 ⅜	14 ⅛
Low	14 ½	13 ⅝	13 ⅞	12 ¼
Dividend Declared	$0.38	$0.38	$0.38	$0.395

Prices shown above are the high and low sale prices, as reported by the Wall Street Journal as composite transactions.

PENDING RATE INCREASE APPLICATIONS

(at December 31, 1980)

	Date Filed	Type	Annual Amount (In Millions)	Where Pending
AP&L	5/29/80	Retail	$130.10	APSC
	8/28/80	Wholesale	$9.97	FERC
ARK-MO	7/23/80	Retail	$7.48	APSC
LP&L	7/29/77	Wholesale	$8.54	FERC
	5/30/80	Retail	$203.60	LPSC
	7/3/80	Retail	$4.44	City Council (NO)
MP&L	12/23/80	Retail-Appealed	$68.77	Chancery Court (Hinds Co., Mississippi)
NOPSI	4/14/80	Retail	$23.28	City Council (NO)
	4/14/80	Retail (gas)	$9.18	City Council (NO)
TOTAL			$465.36	

CUSTOMER INFORMATION

During 1980 System companies began training personnel who will conduct computer-assisted energy audits for homes and businesses.

CUSTOMERS. The System's four operating companies serve some 1.5 million electric customers in parts of Arkansas, Louisiana, Mississippi, and southeast Missouri. Approximately 87 percent are residential customers. During 1980, the number of retail customers (residential, commercial, industrial, and governmental) within the Middle South System grew at a rate of 2.1 percent.

ELECTRIC ENERGY REQUIREMENTS. The summer of 1980 brought record-breaking hot weather conditions which had a significant impact on increasing customers' electric energy requirements. From early July through August, the area served by System companies experienced weather which was marked by sustained and widespread high temperatures unrelieved by significant rainfall or cool intervals.

However, slow-down of the U.S. economy was reflected throughout the service area and tended to reduce energy requirements.

Among the hardest hit industries were forest and allied products (lumber, wood, and paper). The economic slump, in concert with record high interest rates, caused new home construction to be down, hence the decreased demand for wood and other building products. In addition, there were greater curtailments than anticipated in the production of chlorine and refined petroleum products, which require large amounts of energy.

Largely as a result of the extreme summer weather, the System's residential, commercial, industrial, and governmental customers used 5.4 percent more electric energy in 1980 than in 1979. Usage in 1980 was 50.1 billion kilowatt-hours.

Residential customers required 16.1 billion kilowatt-hours during the year, an increase of 10.0 percent. Commercial usage rose 6.0 percent to 9.3 billion kilowatt-hours, and industrial customers used 22.9 billion kilowatt-hours, 2.4 percent more than in 1979. Governmental customers increased their electric energy requirements to 1.8 billion kilowatt-hours, up 2.6 percent from a year ago.

Energy sales to municipalities, rural cooperatives, and other utility systems totaled 5.1 billion kilowatt-hours in 1980, 6.7 percent less than in 1979. This decrease is due in part to the fact that several customers in this category are now part owners in the White Bluff generating station in Arkansas and began receiving part of their energy in 1980 from this new station. These customers will also own part of the Independence generating station when it is completed. The participation of these customers in these new stations has decreased their need to purchase energy from the System.

In 1980, the System's peak demand — the one hour in the year in which customers' greatest requirements for electric energy occur — was 11,769,000 kilowatts. This peak, which occurred on July 16 at 4:00 p.m., was during the hottest part of the extended period of intense summer weather. This was a new record for the System, some 10 percent over the previous year's record peak of 10,687,000 kilowatts.

INDUSTRIAL GROWTH. The System service area has been the beneficiary of a portion of the industrial growth known as the "Sunbelt shift," which describes the movement of business and population from the North to the South.

An important source of regional economic growth is an increase in manufacturing in the region. This increase produces increased employment and higher wages, which attract workers who in turn increase the demand for locally provided goods and services.

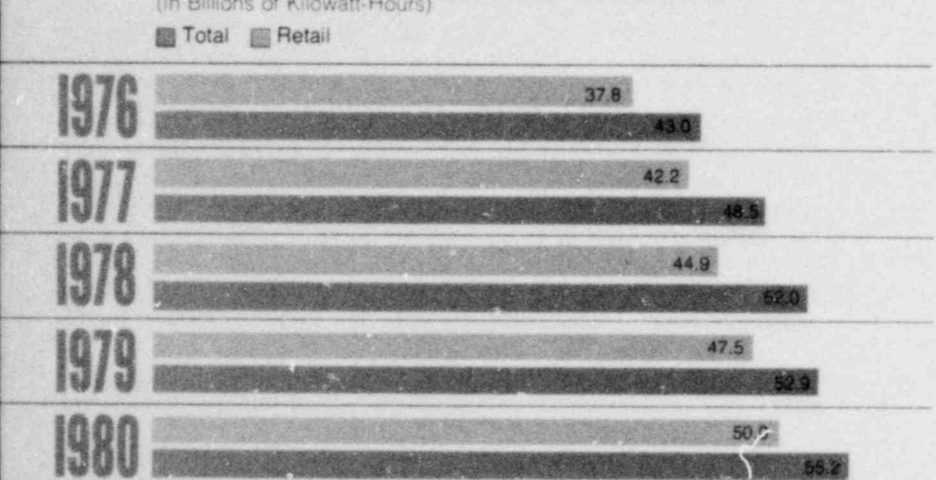
This employment growth leads not only to higher incomes, but more importantly to higher average income per person. The increases in incomes and employment create economic opportunities within the service area. This has reversed the outward migration which was experienced in the 1950s and early 1960s as people sought employment in other parts of the country.

The System companies actively promote the economic and industrial development of their service areas. Although the national economy was characterized as being in recession during a substantial part of 1980, the System service area's Sunbelt location experienced continued, if slower, development.

During 1980, new industrial facilities or expansions numbered some 217 in the Middle South service area, creating 8,876 new jobs and boosting the area's annual payroll by approximately $107 million. Of particular importance to the System companies is the fact that these new or expanded industrial customers will require energy that should produce some $38 million per year in additional System revenues. For the three years prior to 1980, new or expanded industries averaged 237 per year, with an average of 7,681 new jobs and a $72.3 million average yearly addition to the area's payroll.

CUSTOMERS' ENERGY REQUIREMENTS

(in Billions of Kilowatt-Hours)



CONSERVATION & EFFICIENT ENERGY USE. Energy conservation and increased efficiency in the use of energy are important factors in America's energy picture. Avoidance of energy waste has for an increasing segment of our population become a pragmatic as well as an ethical imperative.

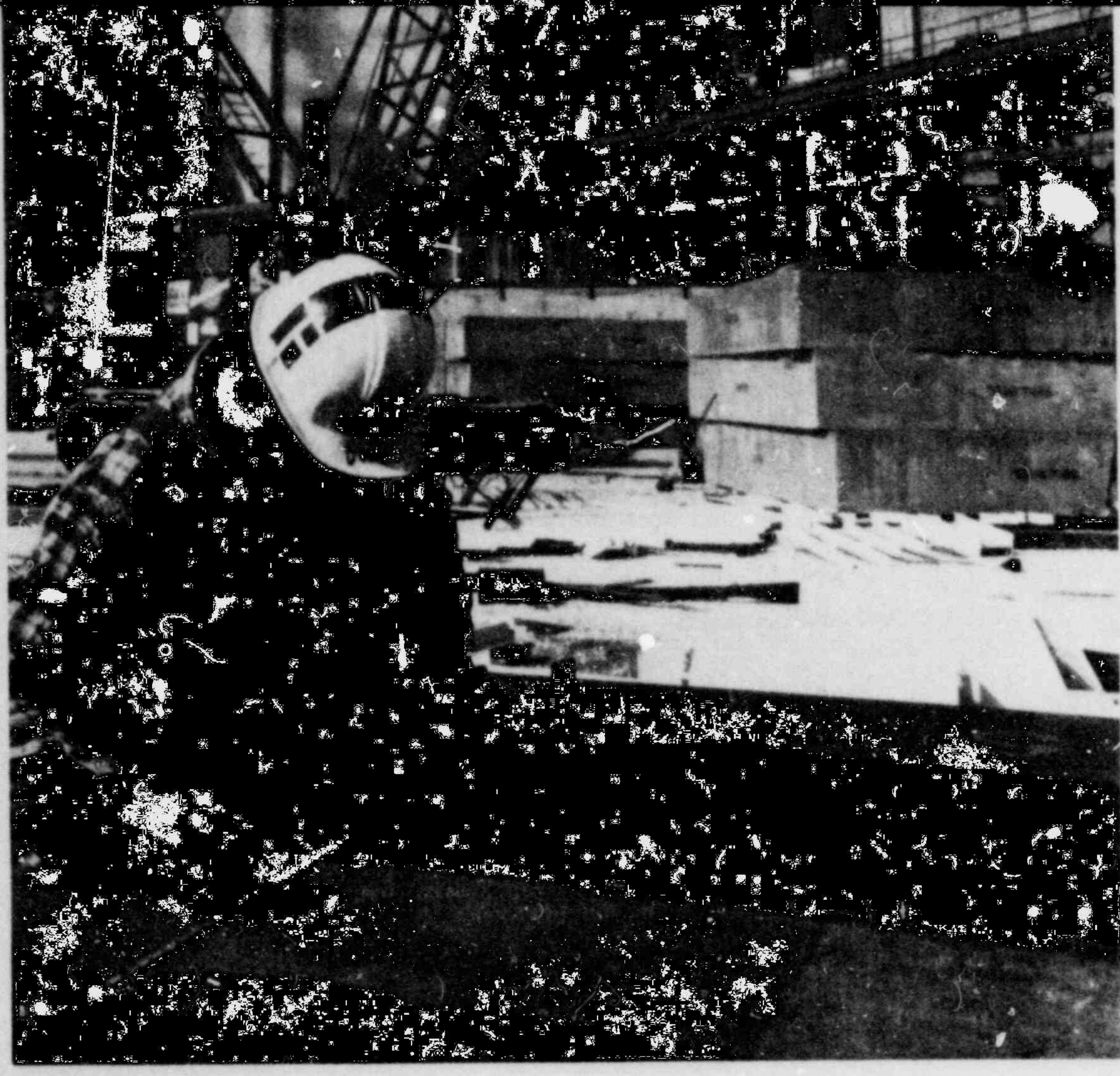
Too great a dependence on foreign sources of oil poses perhaps the greatest security threat to the United States. Studies, both by the System and by objective outside sources, firmly establish that greatly increased use of coal and uranium as fuels for generating electricity will be required in order for America to move in the direction of energy self-sufficiency. Extensive efforts to improve the efficiency of the use of energy resources will also be vital to the success of realistic energy independence efforts.

The Middle South Utilities System has long been a leader in the field of innovative load management and practical customer conservation techniques. Programs designed for the construction of energy-efficient homes and commercial buildings, computer-assisted home energy audits, other consumer-oriented conservation promotions, solar water heaters, and heat-recovery water heaters are among the imaginative, progressive load management ideas that have been conceived and implemented by System companies. These techniques have positive benefits for customers — reducing their energy costs by minimizing the System's use of older "peaking" units which generally have lower efficiencies and require higher-priced fuels.

One way for utilities to achieve this benefit is by improving daily load factor — the degree to which facilities are used relative to their capacity — while minimizing peak load requirements. Customer energy requirements come in "peaks" and "valleys." The customers are best served by utility pursuit of programs that limit the daily peak demands and transfer this energy requirement to periods below the peak daily requirements, where incremental costs of power are normally lower.

An innovative technique utilized by System companies is the radio-controlled switch for air-conditioning compressors. With the incentive of special reduced rates, customers allow their electric utility to remotely turn off their air conditioners for brief intervals during periods of high demand. This reduces peak electrical load requirements without causing undue discomfort to the customer.

AP&L has introduced time-of-day rates for residential customers aimed at causing a shift in some of their use of electricity to periods of lower demand.



CONSTRUCTION, FUEL AND OPERATIONS

Construction progressed during 1980 at LP&L's Waterford 3 nuclear generating plant near Taft, Louisiana, 25 miles up the Mississippi River from New Orleans. The plant was 82 percent complete at the end of 1980.

CONSTRUCTION. Significant milestones were reached during the year in the System's extensive construction program aimed at diversifying the fuel base to lessen dependence on oil and natural gas as fuels for electric generation. During 1980, one nuclear generating unit and one coal-fueled generating unit were placed in commercial operation on the System. Under construction are three more coal-fueled units and three nuclear units, all of which are now scheduled to be in commercial operation by the end of 1986. In addition, the System is planning the installation of six standard-design units in the late 1980s and early 1990s. Some will be coal-fueled and others, lignite-fueled.

System construction expenditures in 1980 totaled some $910 million. Expenditures for new facilities in 1981 are expected to be approximately $897 million.

NUCLEAR UNITS. The System's second nuclear unit, AP&L's Arkansas Nuclear One, unit two, was placed in commercial operation in March 1980. Total cost of this 858,000-kilowatt unit was $632 million.

Three nuclear units remain under construction on the System.

Units one and two at the Grand Gulf nuclear plant near Port Gibson, Mississippi, were 85 percent and 22 percent complete, respectively, at year-end 1980. These units, being built by MP&L as agent for MSE, are scheduled for commercial operation in 1982 and 1986. They will have a capacity of 1,250,000 kilowatts each. In October 1980, an agreement was entered into for the acquisition of a 10-percent undivided ownership interest in the Grand Gulf units by South Mississippi Electric Power Association. Negotiations are currently under way with Municipal Energy Agency of Mississippi for the possible acquisition by that agency of up to a 2.48-percent undivided ownership interest in both units at Grand Gulf. The cost to MSE of its 87.52-percent share of the units is expected to be some $2.85 billion.

Waterford 3, LP&L's nuclear unit, is being built near Taft, Louisiana, 25 miles up the Mississippi River from New Orleans. The unit, with a capacity of 1,104,000 kilowatts, was 82 percent complete at year-end and is expected to go into commercial operation in the first half of 1983. The total cost of that facility will be approximately $1.5 billion.

CONSTRUCTION, FUEL AND OPERATIONS

At the Grand Gulf nuclear generating plant near Port Gibson, Mississippi, Unit 1 reached 85 percent of completion by year-end 1980. Unit 1 is scheduled for commercial operation in 1982.

COAL UNITS. In August, a new fuel era for the Middle South Utilities System was ushered in when AP&L placed in commercial operation the System's first coal-fueled generating unit in modern times. The first unit of AP&L's White Bluff plant has a capacity of 815,000 kilowatts, of which the System has 57 percent ownership. The remaining 43 percent ownership is held by the Arkansas Electric Cooperative Corporation and the cities of Jonesboro, Conway, and West Memphis, Arkansas.

The plant's second unit, of identical design, was 64 percent complete at the end of 1980 and is expected to enter commercial service during the summer of 1981. The System's ownership of this unit is also 57 percent. The cost of AP&L's portion of these two units is expected to total some $426 million.

Two other coal-fueled units, under construction at the Independence Steam Electric Station, are essentially duplicates of the White Bluff units. Construction of the two units, which began in late 1978, was 29 percent and eight percent complete, respectively, at the close of 1980. They are expected to be ready for commercial operation in 1983 and 1985 and together will cost approximately $509 million for the System's 56.5-percent share of their ownership.

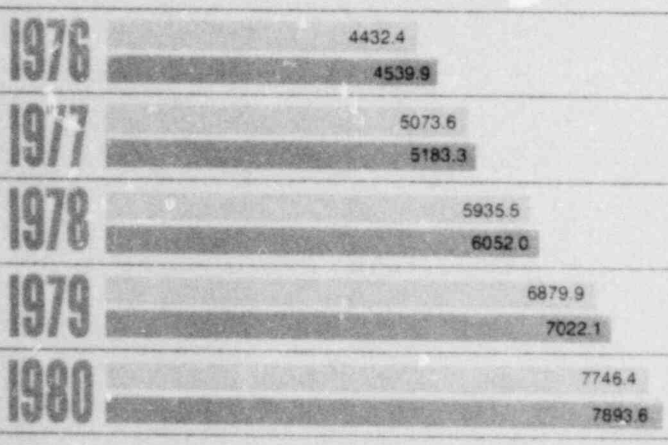
Six additional coal or lignite-fueled units of standard design are planned for operation in the late 1980s and early 1990s. Two units will burn lignite, two will burn low-sulfur coal, and the fuel for the remaining two will be determined at a later date. Each unit will have a nominal capacity of 800,000 kilowatts. The first unit is expected to be built by LP&L in south Louisiana on a Mississippi River site. It is presently slated for commercial operation in 1988.

CONSTRUCTION PROGRAM: MAJOR GENERATING UNITS

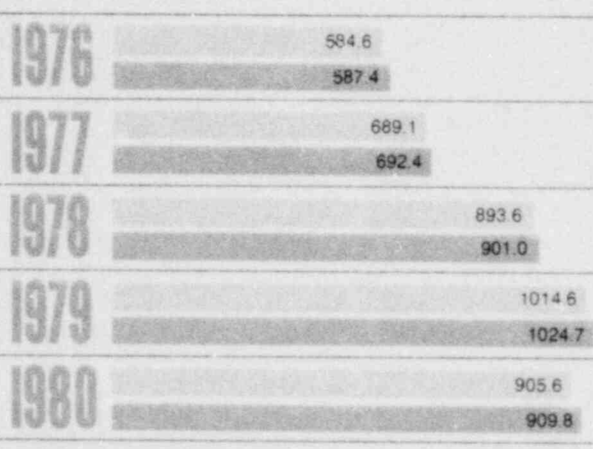
Unit	Company	Fuel	Megawatt (MW) Capacity	Scheduled Commercial Operation
White Bluff #2	AP&L	Coal	465*	1981
Grand Gulf #1	MSE	Nuclear	1,094***	1982
Waterford #3	LP&L	Nuclear	1,104	1983
Independence #1	AP&L	Coal	461**	1983
Independence #2	AP&L	Coal	461**	1985
Grand Gulf #2	MSE	Nuclear	1,094***	1986

*Represents the System's 57% interest in this 815 MW unit.
**Represents the System's 56.5% interest in these 815 MW units.
***Represents the System's 87.5% interest in these 1,250 MW units.

GROSS PLANT (in Millions of Dollars)



CONSTRUCTION EXPENDITURES (in Millions of Dollars)



CONSTRUCTION, FUEL AND OPERATIONS

In an average week, ten unit trains, each with 110 coal cars, deliver their coal to the White Bluff plant site. The plant keeps at least a 60-day coal supply in storage.

FUELS. The necessary diversification of the System's fuel sources, away from historical dependence on natural gas and, later, fuel oil, was begun in the mid-1960s when management made the decision to build a nuclear generating plant. The wisdom of this diversification was underlined during the 1970s when the System began to encounter difficulties not only in obtaining new commitments for long-term supplies of natural gas for power plant boilers but also in receiving deliveries under existing contracts. Some gas-burning facilities were converted to enable them to burn fuel oil. For the foreseeable future, all new base-load generating facilities on the System will be coal, lignite, or nuclear-fueled.

NATURAL GAS AND FUEL OIL. During 1979 and continuing through 1980, the availability of natural gas under short-term interruptible contract was much greater than had been anticipated. This was known as the "gas bubble," a recent phenomenon in the gas marketplace, the expected duration of which is a subject of substantial debate. Although long-range projections of gas availability and pricing confirm the urgency of creating options to dependence on natural gas as a boiler fuel, the System was able during 1979 and 1980 to make economic use of the gas fuel which became available.

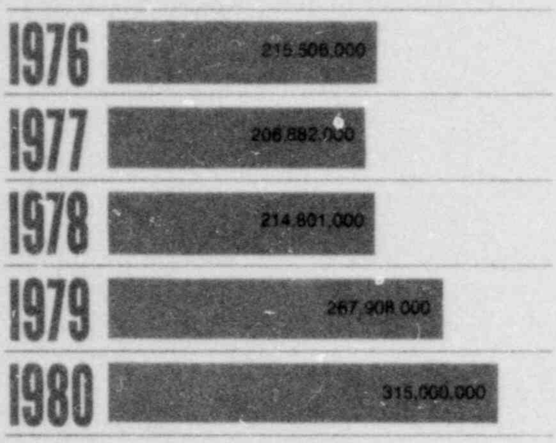
As illustrated in the chart of gas utilization, the amount of gas used in System gas-burning power plants in 1979 and 1980, as measured in millions of cubic feet, increased substantially over the years immediately prior to the "bubble."

The growth of coal and nuclear-fueled electric generation, as a percentage of the System's total fuel mix, resulted in a relative decline in the percentages attributed to gas and fuel oil.

The natural gas used by System companies in 1980 represented the equivalent of some 52 million barrels of increasingly expensive fuel oil. The System used approximately 315,000 million cubic feet of gas in 1980, accounting for 62.9 percent of the fuel mix, as compared with 57 percent in 1979.

The System used approximately 14 million barrels of fuel oil in 1980. This represented about 18 percent of the System's fuel for electric generation, as compared with 33 percent in 1979 and 47 percent in 1978.

NATURAL GAS USAGE (Thousand Cubic Feet)



The System expects to use about 3.3 million barrels of fuel oil in 1981. It has contracts for more than this quantity and will market to other users that which is excess to System requirements. Additional natural gas, as available and when economical, will be used to lessen the System's use of fuel oil.

NUCLEAR FUEL. With commercial operation of the System's second nuclear unit, the nuclear portion of System electric generation climbed from 10 percent in 1979 to 17 percent in 1980.

The System has under contract sufficient uranium to meet all of its nuclear fuel needs through the year 1985.

Seeking supplementary supplies of uranium for future needs, SFI has been conducting a uranium exploration program.

COAL. Coal became a part of the MSU fuel mix in 1980, accounting for two percent of electric generation.

The System transports low-sulfur coal from mines near Gillette, Wyoming, to the White Bluff plant site in Arkansas, using its own fleet of leased rail cars.

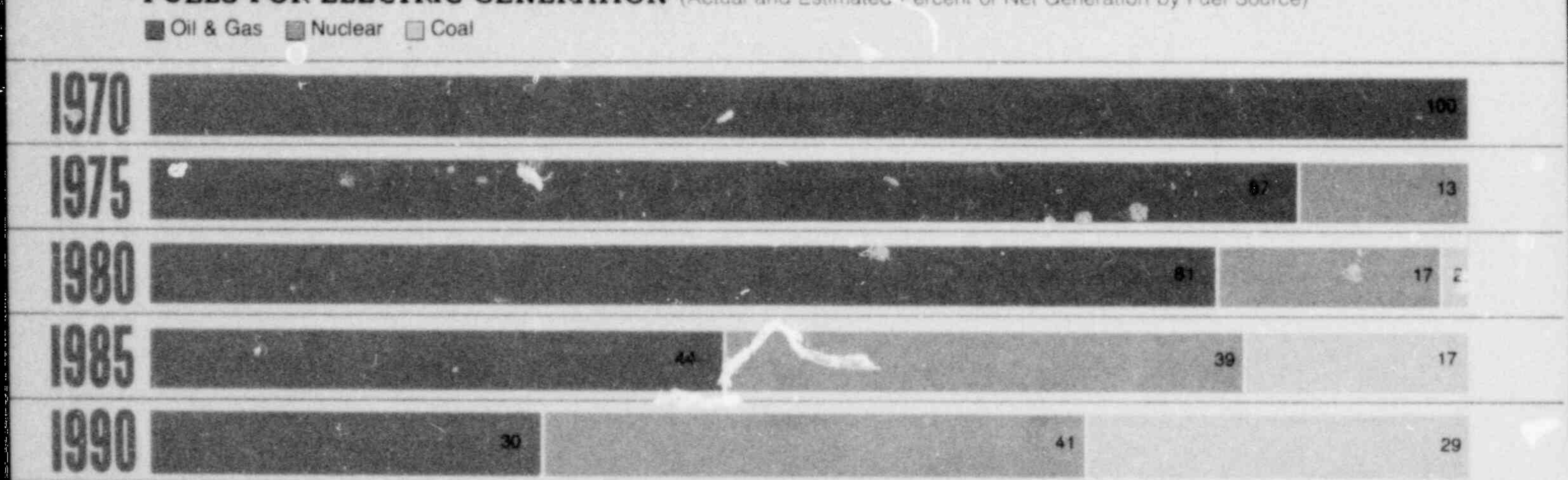
The System has a contract with Kerr-McGee Corporation for the supply of coal to the two White Bluff units which calls for 150 million tons over a projected 30-year life of the units. The two units at AP&L's Independence Station will also use low-sulfur Wyoming coal under another long-term contract with North Antelope Coal Company, which is a joint venture between Powder River Coal Company, a subsidiary of Peabody Coal Company, and Pan Eastern Coal Company, a subsidiary of Panhandle Eastern Pipe Line Company.

The first of the standard-design coal plants, now planned for construction in Louisiana, will burn a low-sulfur Wyoming coal similar to that used at the White Bluff and, later, Independence stations.

Lignite, a low-heat-content form of coal available in Arkansas, will be used as fuel for two future standard-design generating units in Arkansas.

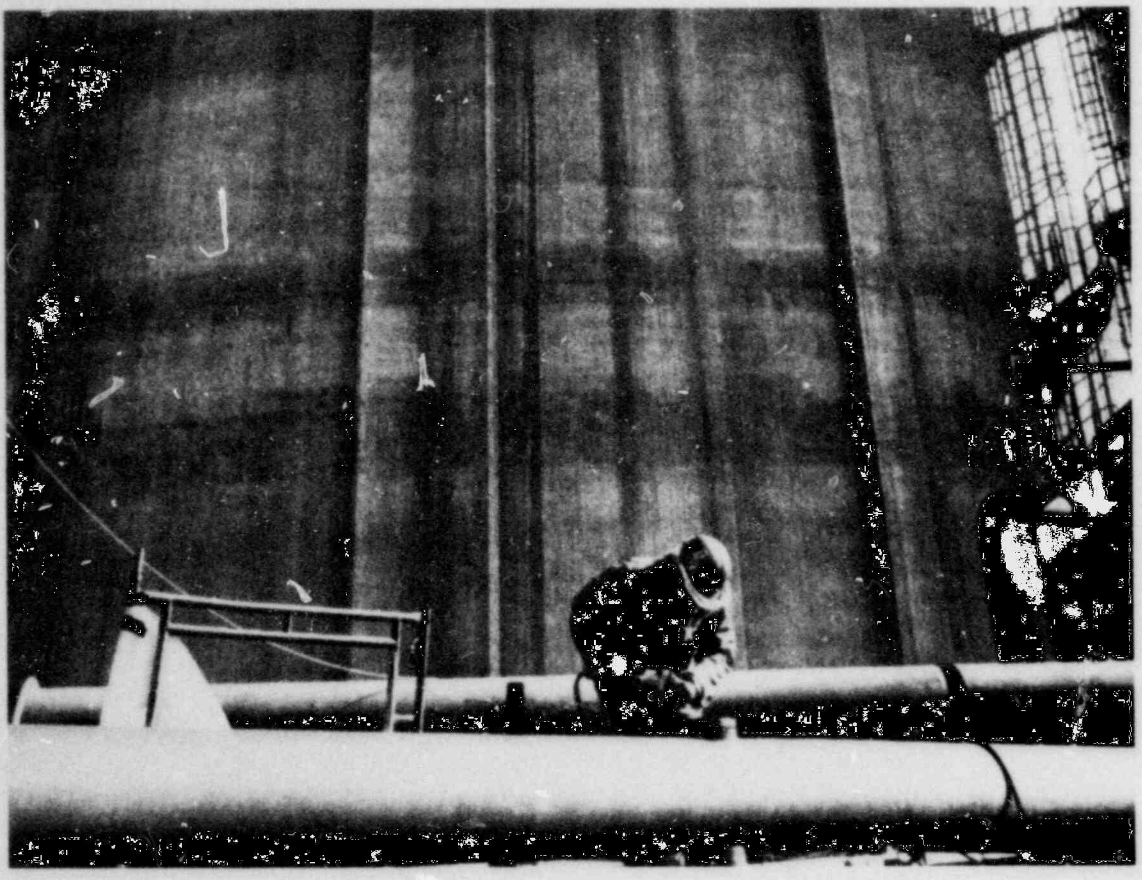
PURCHASED POWER. Through interconnecting ties with other utilities, the Middle South System has access to electric energy other than that generated on our system. The System from time to time can pur-

FUELS FOR ELECTRIC GENERATION (Actual and Estimated Percent of Net Generation by Fuel Source)



Note: Hydro represents 1% or less.

CONSTRUCTION, FUEL AND OPERATIONS



LP&L's Waterford 3, which is scheduled for commercial operation in the first half of 1983, will have a capacity of 1,104,000 kilowatts.

chase limited amounts of such power more economically than it can be generated. In 1980, 22 percent of the System's total energy was purchased from other utilities. Middle South continues to utilize all its resources to serve its customers with the most economical energy available.

FUEL EXPLORATION, RESEARCH & DEVELOPMENT. SFI has the responsibility for finding, purchasing, and delivering fuel for System generating plants.

SFI is involved in gas and oil exploration. During 1980, SFI had varying degrees of participation in the drilling of 21 wells. Of these wells, SFI held a major working interest and acted as operator of eight wells, four of which became commercial producers. Of the remaining 13 wells drilled with other parties as operator, five proved commercially operational. Nine successful wells out of 21 is a high percentage by industry standards.

Work continued in 1980 on SFI's effort to acquire leases of land in southern Louisiana on which to implement its experimental project to extract natural gas from hydropressured salt water formations underlying the Louisiana-Texas coast. Estimates indicate that the gas dissolved in this water may, if commercially recoverable, provide a major new source for domestic gas production for several decades. This extraction experiment still is in the early stages of planning. Its eventual feasibility is not yet proven. Because SFI operates on an at-cost, not-for-profit basis, any benefits realized would accrue to the customers if this experimental project is successful.

The major part of the Middle South System's research and development effort continues to be through the industry-funded Electric Power Research Institute (EPRI), of which MSU Chairman and President Floyd W. Lewis is currently chairman. The System's 1980 contribution, $6.8 million, was used to help fund EPRI's comprehensive research program.

In its recently published five-year Overview and Strategy, EPRI stated that coal, coal-derived synthetic fuels, and uranium must supply the major portion of electricity generated for at least the next two to three decades. Even with a rapid increase in coal-fired generation, according to EPRI, 10 to 25 percent of America's electricity needs could be unfilled in the year 2000 unless nuclear power fills the gap, making nuclear power "not a question of preference, but a matter of necessity."

REPORT OF MANAGEMENT

The management of Middle South Utilities, Inc., has prepared and is responsible for the financial statements and related financial information included in this annual report. The financial statements are based on generally accepted accounting principles, consistently applied. Financial information included elsewhere in this report is consistent with the financial statements.

To meet its responsibilities with respect to financial information, management maintains and enforces a system of internal accounting controls which is designed to provide reasonable assurance, on a cost effective basis, as to the integrity, objectivity and reliability of the financial records and as to the protection of assets. This system includes communication through written policies and procedures, and an organizational structure that provides for appropriate division of responsibility and the training of personnel. This system is also tested by a comprehensive internal audit program.

The board of directors pursues its responsibility for reported financial information through its audit committee, composed of outside directors. The audit committee meets periodically with management, the internal auditors, and the independent public accountants to discuss auditing, internal control, and financial reporting matters. The independent public accountants have free access to the audit committee at any time.

The independent public accountants provide an objective assessment of the degree to which management meets its responsibility for fairness of financial reporting. They regularly evaluate the system of internal accounting control and perform such tests and other procedures as they deem necessary to reach and express an opinion on the fairness of the financial statements.

We believe that these policies and procedures provide reasonable assurance that our operations are carried out with a high standard of business conduct.

AUDITORS' OPINION

The Stockholders and the Board of Directors
of Middle South Utilities, Inc.:

We have examined the consolidated balance sheets of Middle South Utilities, Inc. and its subsidiaries as of December 31, 1980 and 1979 and the related consolidated statements of income, retained earnings, paid-in capital, and changes in financial position for each of the three years in the period ended December 31, 1980. 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 above-mentioned consolidated financial statements present fairly the financial position of the Company and its subsidiaries at December 31, 1980 and 1979 and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1980, in conformity with generally accepted accounting principles applied on a consistent basis.

Deloitte Haskins + Sells

New Orleans, Louisiana
February 13, 1981

STATEMENTS OF CONSOLIDATED INCOME
For the Years Ended December 31, 1980, 1979 and 1978

	1980	1979	1978
		(In Thousands)	
Operating Revenues (Note 2):			
Electric	$2,181,320	$1,669,451	$1,489,915
Natural gas	116,796	116,612	95,863
Transit	44,112	36,996	36,399
Total	2,342,228	1,823,059	1,622,177
Operating Expenses:			
Operation:			
Fuel for electric generation	946,145	697,606	623,402
Purchased power	281,951	258,377	133,929
Gas purchased for resale	88,864	88,801	68,657
Other	283,905	200,264	199,406
Maintenance	111,831	111,394	99,941
Depreciation	141,997	119,304	112,805
Taxes other than income taxes	84,890	77,849	69,771
Income taxes (Note 3)	105,023	51,266	86,004
Total	2,044,406	1,604,861	1,393,915
Operating Income	297,822	218,198	228,262
Other Income:			
Allowance for equity funds used during construction (Note 1G)	122,277	124,086	93,573
Miscellaneous income and deductions - net	7,019	7,940	6,239
Income taxes - cr. (Note 3)	106,284	76,232	50,105
Total	235,580	208,258	149,917
Interest and Other Charges:			
Interest on long-term debt	327,468	255,242	199,212
Other interest - net	72,666	42,139	22,769
Allowance for borrowed funds used during construction - cr. (Note 1G)	(117,663)	(89,247)	(54,717)
Preferred dividend requirements of subsidiaries (Note 6)	55,024	36,264	25,477
Total	337,495	244,398	192,741
Net Income (Note [illegible])	$ 195,907	$ 182,058	$ 185,458
Earnings Per Common Share	$2.01	$2.13	$2.46
Dividends Declared Per Common Share	$1.59	$1.535	$1.46
Average Number of Common Shares Outstanding	97,459,169	85,444,691	75,522,179

See Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS December 31, 1980 and 1979

ASSETS

	1980	1979
	(In Thousands)	
Utility Plant (Notes 9 and 10):		
Electric	$4,603,155	$3,597,923
Natural gas	105,911	102,878
Transit	17,535	19,049
Construction work in progress	3,167,035	3,282,202
Total	7,893,636	7,002,052
Less - Accumulated depreciation	1,264,525	1,139,164
Utility plant - net	6,629,111	5,862,888
Other Property and Investments	90,012	91,806
Current Assets:		
Cash (Note 4)	58,565	52,038
Special deposits	16,638	13,341
Temporary investments - at cost, which approximates market	69,817	69,839
Notes receivable	2,470	17,706
Accounts receivable:		
Customer (less allowance for doubtful accounts of (in thousands) $2,253 in 1980 and $1,800 in 1979)	123,207	101,148
Other	35,507	22,197
Deferred fuel cost	25,675	28,929
Fuel inventory - at average cost (Note 4)	153,334	137,058
Materials and supplies - at average cost	36,168	36,488
Other	26,223	21,744
Total	547,604	500,488
Deferred Debits	68,152	47,886
TOTAL	$7,334,879	$6,503,068

See Notes to Consolidated Financial Statements.

CAPITALIZATION AND LIABILITIES

	1980	1979
	(In Thousands)	
Capitalization:		
Common stock, $5 par value, authorized 150,000,000 shares; issued and outstanding 107,349,943 shares in 1980 and 90,432,998 shares in 1979 (Note 5)	$ 536,750	$ 452,165
Paid-in capital	749,206	630,450
Retained earnings (Note 8)	619,572	581,445
Total common shareholders' equity	1,905,528	1,664,060
Subsidiaries' preferred stock, without sinking fund (Note 6)	330,967	330,967
Subsidiaries' preferred stock, with sinking fund (Note 6)	283,165	193,507
Long-term debt (Note 7)	3,392,309	3,017,816
Total	5,911,969	5,206,350
Current Liabilities:		
Notes payable (Notes 4 and 9):		
Banks	187,494	264,275
Commercial paper	16,750	20,630
Other	91,378	—
Currently maturing long-term debt	121,473	149,830
Accounts payable	276,991	210,123
Customer deposits	37,870	33,289
Taxes accrued	67,401	55,435
Accumulated deferred income taxes (Note 3)	14,602	14,950
Interest accrued	81,984	75,737
Dividends declared	58,372	47,594
Other	43,555	25,679
Total	997,670	897,542
Deferred Credits:		
Accumulated deferred income taxes (Note 3)	255,572	257,599
Accumulated deferred investment tax credits (Note 3)	101,137	104,835
Other	43,679	17,282
Total	400,388	379,716
Reserves	24,652	19,460
Commitments and Contingencies (Notes 2, 9 and 10)		
TOTAL	$7,334,879	$6,503,068

STATEMENTS OF CONSOLIDATED RETAINED EARNINGS AND PAID-IN CAPITAL For the Years Ended December 31, 1980, 1979 and 1978

RETAINED EARNINGS

	1980	1979	1978
		(In Thousands)	
Retained Earnings, January 1	$581,445	$534,893	$460,608
Add - Net income	195,907	182,058	185,438
Total	777,352	716,951	646,04[illegible]
Deduct:			
Dividends declared on common stock - $1.59, $1.535 and $1.46 per share for 1980, 1979 and 1978, respectively	156,968	132,585	110,849
Capital stock expenses, etc.	812	2,921	304
Total	157,780	135,506	111,153
Retained Earnings, December 31 (Note 8)	$619,572	$581,445	$534,893

PAID-IN CAPITAL

	1980	1979	1978
Paid-in Capital, January 1	$630,450	$499,855	$401,156
Add:			
Excess of proceeds over par value:			
Public sales of common stock:			
8,000,000 shares in October 1980	54,023	—	—
7,000,000 shares in May 1980	50,819	—	—
5,000,000 shares in November 1979	—	38,099	—
8,500,000 shares in January 1979	—	84,490	—
8,500,000 shares in January 1978	—	—	94,460
Common stock issued in connection with dividend reinvestment and stock purchase plan	11,029	5,865	4,053
Common stock issued in connection with employee stock ownership plan	74	126	54
Common stock issued in connection with employee savings plan	2,202	2,021	132
Other	609	(6)	—
Paid-in Capital, December 31	$749,206	$630,450	$499,855

See Notes to Consolidated Financial Statements.

STATEMENTS OF CHANGES IN CONSOLIDATED FINANCIAL POSITION For the Years Ended December 31, 1980, 1979 and 1978

	1980	1979	1978
		(In Thousands)	
Funds Provided By:			
Operations:			
Net income	$ 195,907	$ 182,058	$ 185,438
Depreciation	141,997	119,304	112,805
Amortization of property loss	—	4,101	4,101
Deferred income taxes and investment tax credit adjustments - net	(6,060)	(24,856)	36,427
Allowance for funds used during construction (Note 1G)	(239,940)	(213,333)	(148,290)
Total funds provided by operations	91,904	67,274	190,481
Other:			
Allowance for funds used during construction (Note 1G)	239,940	213,333	148,290
Advance for non-utility property	—	14,737	—
Decrease in working capital*	70,830	—	—
Miscellaneous - net	17,206	—	7,573
Total funds provided by operations and other	419,880	295,344	346,344
Financing and other transactions:			
Common stock	202,732	202,269	143,147
Preferred stock	93,444	183,699	—
First mortgage bonds	218,500	160,000	242,000
Promissory notes and other long-term debt	282,626	378,863	235,623
Book value of utility plant sold	934	9,547	—
Short-term securities - net	10,739	—	135,575
Sale and leaseback transactions	45,484	24,652	—
Total funds provided by financing and other transactions	854,459	959,030	756,345
Total funds provided	$1,274,339	$1,254,374	$1,102,689
Funds Applied To:			
Utility plant additions:			
Construction expenditures for utility plant	$ 909,844	$1,024,743	$ 900,907
Expenditures for nuclear fuel	26,288	(17,229)	701
Other - net	4,219	(1,718)	(18,103)
Total gross additions (includes allowance for funds used during construction of (in thousands) $239,940 in 1980, $213,333 in 1979 and $148,290 in 1978)	940,351	1,005,796	883,505
Dividends declared on common stock	156,968	132,585	110,849
Retirement of promissory notes and other long-term debt	129,586	3,313	2,177
Retirement of first mortgage bonds	24,081	19,802	27,854
Retirement of preferred stock	3,787	—	—
Repayment of short-term securities - net	—	43,849	—
Increase in working capital*	—	12,637	52,754
Deferred costs on coal plant standardization study	5,749	6,776	1,781
Deferred costs relating to SFI's fuel acquisition program for:			
Oil and gas	1,908	9,163	3,962
Uranium	8,051	8,487	2,232
Coal	3,858	4,085	2,838
Advance for non-utility property	—	—	14,737
Miscellaneous - net	—	7,881	—
Total funds applied	$1,274,339	$1,254,374	$1,102,689

**Working capital does not include short-term securities, current maturities of long-term debt or deferred taxes included in current liabilities. The 1980 net decrease in working capital is primarily due to increases in accounts payable and other current liabilities reduced by an increase in customer accounts receivable, while the 1979 net increase is primarily due to increases in accounts receivable and fuel oil inventory reduced by an increase in accounts payable, and the 1978 net increase is primarily due to an increase in cash and special deposits and a decrease in taxes accrued.*

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of Middle South Utilities, Inc. (the Company) and its direct and indirect subsidiaries, Arkansas Power & Light Company (AP&L), Arkansas-Missouri Power Company (Ark-Mo), Louisiana Power & Light Company (LP&L), Mississippi Power & Light Company (MP&L), New Orleans Public Service Inc. (NOPSI), Middle South Services, Inc. (MSS), Middle South Energy, Inc. (MSE) and System Fuels, Inc. (SFI) which are collectively referred to as the System Companies or the Middle South System. All significant intercompany transactions have been eliminated.

B. SYSTEMS OF ACCOUNTS

The accounts of the Company and its service subsidiary are maintained in accordance with the Public Utility Holding Company Act of 1935, as administered by the Securities & Exchange Commission, which has adopted the systems of accounts prescribed by the Federal Energy Regulatory Commission (FERC).

The accounts of the operating subsidiaries and the generating subsidiary are maintained in accordance with the systems of accounts prescribed by the applicable regulatory bodies, which systems of accounts substantially conform to those prescribed by the FERC. NOPSI operates pursuant to ordinances and orders of the Council of the City of New Orleans relating to regulation, supervision and control. Under these ordinances the City has an option to purchase that company's properties and operations.

SFI capitalizes all costs related to its exploration activities. These costs are amortized by the unit-of-production method in the period in which revenue is recognized on oil and gas reserves produced and sold.

C. REVENUES AND FUEL COSTS

The operating subsidiaries record electric and gas revenues as billed to their customers on a cycle billing basis. Revenue is not accrued for energy delivered but not billed at the end of the fiscal period. Substantially all of the rate schedules of the operating subsidiaries include adjustment clauses under which the cost of fuel used for generation and gas purchased for resale above or below specified base levels is permitted to be billed or required to be credited to customers.

Two operating subsidiaries have fuel adjustment clauses which allow current recovery of fuel costs. Prior to 1978 two others had adopted a deferral method of accounting for those fuel costs recoverable under fuel adjustment clauses. Under this method such costs are deferred until the related revenues are billed. Effective January 1, 1979, pursuant to an order by its regulatory commission, the remaining operating subsidiary commenced deferring fuel costs recoverable under its fuel adjustment clauses, the effect of which was to increase net income (net of deferred income taxes) by $1,033,000 and $7,765,000 in 1980 and 1979, respectively.

The fuel adjustment clause for AP&L contains a provision for a nuclear reserve fund to cover the estimated costs of replacement energy when the nuclear plant is down for scheduled maintenance and refueling. The fund bears interest and is credited to the fuel and purchased power expenses during the shutdown period.

D. UTILITY PLANT AND DEPRECIATION

Utility plant is stated at original cost. The cost of additions to utility plant includes contracted work, direct labor and materials, allocable overheads and an allowance for the composite cost of funds used during construction. The costs of units of property retired are removed from utility plant and such costs, plus removal costs, less salvage, are charged to accumulated depreciation. Maintenance and repairs of property and replacement of items determined to be less than units of property are charged to operating expenses.

Depreciation is computed on the straight-line basis at rates based on the estimated service lives of the various classes of property. Depreciation rates for AP&L's nuclear plant include a provision for nuclear plant decommissioning costs. Depreciation provisions on average depreciable property approximated 3.4%, 3.5% and 3.4% in 1980, 1979 and 1978, respectively.

Substantially all of the utility plant of the Company's operating subsidiaries and generating subsidiary is subject to the liens of their respective first mortgage bond indentures.

E. PENSION PLANS

The Company and its subsidiaries have various pension plans covering substantially all of their employees. The policy of the Company and its subsidiaries is to fund pension costs accrued.

F. INCOME TAXES

The Company and its subsidiaries file a consolidated Federal income tax return. Income taxes are allocated to all subsidiaries based on their contributions to the consolidated tax liability. Deferred income taxes are provided for differences between book and taxable income to the extent permitted by the regulatory bodies for ratemaking purposes. Investment tax credits utilized are deferred and amortized based upon the average useful life of the related property.

G. ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION

To the extent that the Company's operating subsidiaries are not permitted by their regulatory bodies to recover in current rates the carrying cost of funds used for construction, they capitalize, as an appropriate cost of utility plant, an allowance for funds used during construction (AFDC) which is calculated and recorded as provided by the regulatory system of accounts. Under this utility industry practice, construction work in progress on the balance sheet is charged and the income statement is credited for the approximate net composite interest cost of borrowed funds and for a reasonable return on the equity funds used for construction. This procedure is intended to remove from the income statement the effect of the cost of financing the construction program and results in treating the AFDC charges in the same manner as construction labor and material costs. As non-cash items, these credits to the income statement have no effect on current cash earnings. After the property is placed in service the AFDC charged to construction costs is recoverable from customers through depreciation provisions included in rates charged for utility service. The effective composite AFDC rate for the Company's operating subsidiaries was 7.5% and 7.2% for 1979 and 1978, respectively. During 1980, one of the operating subsidiaries used an accrual rate of 5% on $736.2 million of construction costs in accordance with a December 1979 rate order from its regulatory commission. The effective composite rate of the operating subsidiaries for the balance of AFDC was 8.0% for 1980.

MSE has determined its accrual rate for allowance for funds used during construction based on a return on average common equity of 11.6% through October 1980 and 13.75% thereafter, plus actual interest costs, net of related income taxes.

The Company's subsidiaries continue to capitalize allowance for funds used during constuction on projects during periods of interrupted construction when such interruption is temporary and the continuation can be justified as being reasonable under the circumstances.

H. RESERVES

It is the policy of the Company's operating subsidiaries to provide reserves for uninsured property risks and for claims for injuries and damages through charges to operating expense on an accrual basis. Accruals for these reserves have been allowed for ratemaking purposes.

NOTE 2. RATE MATTERS

In May 1980 AP&L filed with the Arkansas Public Service Commission (APSC) an application to increase, through a two-stage process, its retail rates approximately $130 million on an annual basis. On October 28, 1980, AP&L placed into effect, subject to refund, approximately $86.7 million of the increase; operating revenues for 1980 include approximately $10.7 million from the increased rates. The balance of the requested increase, approximately $43.4 million, is proposed to be implemented on June 1, 1981. In a pre-hearing stipulation agreement between AP&L and the APSC staff, the APSC staff recommended an increase of approximately $90 million and, in return, AP&L agreed not to contest certain staff adjustments which would have the effect of reducing AP&L's request from $130 million to approximately $117 million. The matter is pending before the APSC.

In May 1980 MP&L filed with the Mississippi Public Service Commission (MPSC) a notice of intention to change rates in order to produce additional annual revenues of approximately $68.8 million. The proposed rates were put into effect, under bond, on July 1, 1980. On November 24, 1980, the MPSC issued its order authorizing MP&L to file new rates that would produce additional annual revenues of approximately $48.3 million. This decision was appealed by several parties seeking modifications to the MPSC's order. In MP&L's opinion, based on the opinion of legal counsel, these appeals will not be successful. MP&L is requesting that the full rate increase sought be allowed, appealing the MPSC's decision on rate of return,

the disallowance of CWIP in rate base, and the disallowance of a portion of the working capital requested. MP&L is continuing to bill customers using the rates filed in May 1980 pending final determination of these appeals. In 1980 these rates produced an additional $33 million in revenue. The portion of this amount that would have been billed under the rates approved by the MPSC, $23 million, was included in operating revenues. The remainder, $10 million, was recorded as a liability.

As of December 31, 1980, LP&L had pending $216.5 million of proposed annual rate increases, including a general rate increase application filed in May 1980 with respect to customers under the Louisiana Public Service Commission (LPSC) jurisdiction in the amount of $203.6 million. In connection therewith, in October 1980 the LPSC permitted LP&L to implement an interim rate increase of approximately $32.4 million under protective bond, subject to refund. Included in operating revenues for the year 1980 is approximately $8 million of such revenues subject to refund.

NOTE 3. INCOME TAXES

Income tax expense (credit) consists of the following:

	1980	1979	1978
	(In Thousands)		
Current:			
Federal	—	$ (1,475)	$ (3,275)
State	$ 4,799	1,365	2,747
Total	4,799	(110)	(528)
Deferred - net:			
Liberalized depreciation	33,994	40,639	34,411
Deferred fuel cost	(582)	11,215	(540)
Taxes capitalized in the financial statements	6,985	8,153	4,022
Difference between book and tax gains and losses on sales and abandonment of property	(5,753)	(3,527)	(1,794)
Other	(15,992)	9,483	10,981
Reduction due to tax loss carryforwards	(21,027)	(88,253)	(6,487)
Total	(2,375)	(22,290)	40,593
Investment tax credit adjustments - net	(3,685)	(2,566)	(4,166)
Total income taxes	$ (1,261)	$(24,966)	$35,899
Charged to operations	$105,023	$ 51,266	$86,004
Credited to other income	(106,284)	(76,232)	(50,105)
Total income taxes	$ (1,261)	$(24,966)	$35,899

Total income taxes differ from the amounts computed by applying the statutory Federal income tax rate to income before taxes. The reasons for the differences are as follows:

	1980		1979		1978	
			(In Thousands)			
	Amount	% of Pre-Tax Income	Amount	% of Pre-Tax Income	Amount	% of Pre-Tax Income
Computed at statutory rate	$114,848	46.0	$ 88,944	46.0	$118,471	48.0
Increases (reductions) in tax resulting from:						
Allowance for funds used during construction	(110,372)	(44.2)	(98,133)	(50.8)	(71,180)	(28.9)
Difference between book depreciation and tax straight-line depreciation	1,170	0.5	(7,593)	(3.9)	(3,207)	(1.3)
Other - net	(6,907)	(2.8)	(8,184)	(4.2)	(8,185)	(3.3)
Recorded income taxes	$ (1,261)	(0.5)	$(24,966)	(12.9)	$ 35,899	14.5

The tax effects of the consolidated 1980, 1979 and 1978 Federal tax losses of $259,674,000 have been recorded as reductions of deferred income taxes. Unused investment tax credits at December 31, 1980, amounted to $291,276,000 of which $34,939,000 may be carried forward through 1984, $92,966,000 through 1985, $100,502,000 through 1986, and $62,869,000 through 1987.

NOTE 4. LINES OF CREDIT AND RELATED BORROWINGS

The Company and MSE have revolving credit agreements with various banks providing for the issuance of unsecured promissory notes totalling $230 million and $808 million, respectively. The Company's agreement will terminate December 31, 1984, and the maximum principal amount of allowable borrowings will be reduced to 75% and 50% of the original commitment on December 31, 1982, and December 31, 1983, respectively. MSE's agreement expires, and all notes thereunder mature, December 31, 1985. Under both of these agreements commitment fees are paid on the unused portion of the credit lines. In addition, MSE's agreement requires compensating balances.

The operating subsidiaries have arrangements, not requiring commitment fees, with various banks providing for short-term borrowings through bank loans and with commercial paper dealers for the sale of commercial paper. Of the total bank lines of credit, $253 million is provided by banks located outside of the Middle South System service area. Any of the four participating System operating companies may borrow any portion of these lines subject only to each company's maximum authorized level of borrowings. Compensating balances are required by certain of the lending banks.

The short-term loan agreements for MSS ($30 million) and MSE ($60 million) require commitment fees on the unused portions of the lines of credit and compensating balances are required for MSE.

SFI has a fuel oil financing arrangement allowing for borrowings up to $100 million subject to a limit equivalent to the lower of the cost or the fair market value of SFI's fuel oil inventory. In addition, SFI may borrow up to $60 million through the sale of commercial paper for use in financing its nuclear fuel inventory. Borrowings under these arrangements are restricted as to use and are secured respectively by SFI's fuel oil and nuclear fuel inventories and accounts receivable arising from the sale of these inventories. SFI also has a revolving bank credit agreement which allows for borrowings up to $60 million subject to a limit equivalent to 85% of the net book value of certain assets. A commitment fee is paid on the unused portion of this line of credit.

The lines of credit, borrowings and compensating balances of the System companies were as follows:

	December 31, 1980			December 31, 1979		
	Line of Credit	Borrowings	Compensating Balance	Line of Credit	Borrowings	Compensating Balance
	(In Thousands of Dollars)					
Short-term:						
Company	—	—	—	226,820	145,900	—
MSE	60,000	38,151	1,800	60,000	—	1,800
SFI	160,000	108,128	—	110,000	17,500	—
MSS	30,000	14,650	—	—	—	—
Operating subsidiaries	393,085	94,593	15,069	332,000	121,505	20,718
Long-term:						
Company	230,000	108,150	—	—	—	—
MSE	808,000	671,000	33,550	565,000	547,000	27,350
SFI	60,000	18,900	—	115,000	103,590	—
MSS	—	—	—	10,000	4,000	—

The short-term borrowings and the interest rates for the Middle South System were as follows:

	Year Ended December 31,		
	1980	1979	1978
	(In Thousands)		
Average Borrowing	$340,245	$316,061	$199,773
Maximum Borrowing	$469,740	$398,015	$323,440
Year-end Borrowing	$295,622	$284,905	$323,440
Average interest rate:			
During period -			
Bank loans	14.9%	13.6%	10.0%
Commercial paper	14.4%	11.7%	8.6%
Other	12.7%	—	—
At end of period -			
Bank loans	21.4%	[illegible]	12.1%
Commercial paper	20.6%	15.4%	10.8%
Other	19.9%	—	—

NOTE 5. COMMON STOCK

Changes in shares of the common stock of the Company for 1980, 1979 and 1978 were:

Type of Transaction	Number of Shares 1980	1979	1978
Sales	15,000,000	13,500,000	8,500,000
Dividend reinvestment and stock purchase plan	1,604,174	608,875	372,110
Employee stock ownership plan	11,487	12,452	4,825
Employee savings plan	301,284	214,433	12,687
Retirement of unclaimed shares	—	(994)	—
	16,916,945	14,334,766	8,889,622

In January 1981 the Company issued 589,409 shares of its common stock under the Dividend Reinvestment and Stock Purchase Plan. The Company is also seeking authorization from the Securities and Exchange Commission to issue and sell up to 10,000,000 shares of its common stock in the second quarter of 1981 with the proceeds being used primarily to reduce the Company's outstanding bank borrowings at that time.

NOTE 6. PREFERRED STOCK

The number of shares of preferred stock of the operating subsidiaries as of the end of the last two fiscal years were as follows:

	Shares Authorized at December 31, 1980	Shares Outstanding at December 31, 1980	1979	Call Price Per Share
Cumulative, $100 Par Value				
Without sinking fund:				
4.16 - 5.56%	1,070,774	1,070,106	1,070,106	$102.50 to $107.00
6.08 - 8.56%	1,180,000	1,180,000	1,180,000	$102.83 to $107.70
9.16 - 11.48%	795,000	795,000	795,000	$106.35 to $113.98
	3,045,774	3,045,106	3,045,106	
With sinking fund:				
10.60 - 11.04%	562,134	562,134	600,000	$109.39 to $109.78
15.44%	150,000	150,000	—	$115.44
	712,134	712,134	600,000	
Unissued	5,756,500			
Total	9,514,408			
Cumulative, $25 Par Value				
Without sinking fund:				
8.84%	400,000	400,000	400,000	$ 28.21
10.40%	600,000	600,000	600,000	$ 28.60
	1,000,000	1,000,000	1,000,000	
With sinking fund:				
9.92%	1,600,000	1,600,000	1,600,000	$ 28.18
10.72%	2,400,000	2,400,000	2,400,000	$ 27.68
13.12%	1,600,000	1,600,000	1,600,000	$ 28.28
13.28%	2,000,000	2,000,000	—	$ 29.58
15.20%	1,200,000	1,200,000	—	$ 28.80
	8,800,000	8,800,000	5,600,000	
Unissued	12,200,000			
Total	22,000,000			

Changes in the number of shares of preferred stock of the operating subsidiaries during the last two fiscal years (there were no changes in 1978) were as follows:

	Number of Shares 1980	1979
Sales:		
AP&L		
10.40%, $25 par, with sinking fund	—	600,000
9.92%, $25 par, with sinking fund	—	1,600,000
13.28%, $25 par, with sinking fund	2,000,000	—
LP&L		
11.48%, $100 par, without sinking fund	—	350,000
10.72%, $25 par, with sinking fund	—	2,400,000
13.12%, $25 par, with sinking fund	—	1,600,000
15.20%, $25 par, with sinking fund	1,200,000	—
NOPSI		
15.44%, $100 par, with sinking fund	150,000	—
Redemptions:		
AP&L		
11.04%, $100 par, with sinking fund	(20,000)	—
10.60%, $100 par, with sinking fund	(17,866)	—
	3,312,134	6,550,000

The amounts of preferred stock of the operating subsidiaries as of the end of the last two fiscal years were as follows:

	December 31, 1980	1979
	(In Thousands)	
Without sinking fund:		
Stated at $100 a share	$304,511	$304,511
Stated at $25 a share	25,000	25,000
Premium	1,456	1,456
Total without sinking fund	$330,967	$330,967
With sinking fund:		
Stated at $100 a share	$ 71,213	$ 60,000
Stated at $25 a share	220,000	140,000
Premium	852	517
Issuance expense	(8,900)	(7,010)
Total with sinking fund	$283,165	$193,507
Annual preferred stock dividend requirements	$ 59,909	$ 46,703
Average annual preferred stock dividend rate on par value	9.64%	8.82%

Cash sinking fund requirements for the ensuing five years for the preferred stock outstanding at December 31, 1980, are as follows (in thousands): 1981, $3,000; 1982, $3,000; 1983, $3,000; 1984, $10,000; and 1985, $14,750.

NOTE 7. LONG-TERM DEBT

The long-term debt of the Company and its subsidiaries as of the end of the last two fiscal years was as follows:

	Outstanding at December 31 1980	Outstanding at December 31 1979
	(In Thousands)	
First Mortgage Bonds	$2,421,451	$2,321,632
Debentures - due 1983-1993, 5⅞ - 7%	—	3,840
Promissory Notes:		
Due:		
1982, at prime plus ½ of 1%	1,023	1,527
1982, at prime	18,900	—
1984, at 105% of prime plus ¼ of 1%	108,150	—
1985, at 110% of the sum of prime and ¾ of 1%	671,000	547,000
Total Promissory Notes	799,073	548,527
Other:		
Capitalized Lease - due serially through 1993, 8%	7,292	7,648
Municipal Revenue Bonds - due serially through 2004, 1¼ - 8%	41,421	39,473
Pollution Control Revenue Bonds and Installment Purchase Contracts:		
Due serially through 2009, 6 - 8%	17,350	17,451
Due 1995 - 2008, 6⅛ - 10%	111,425	94,625
Less - Funds on deposit with trustee	(8,580)	(19,580)
Total Other	168,908	139,617
Unamortized Premium and Discount - Net	2,977	4,200
Total Long-Term Debt	$3,392,309	$3,017,816
Annual interest requirements on Long-Term Debt	$ 429,903	$ 298,277
Average annual interest rate on total Long-Term Debt (excluding unamortized premium and discount - net)	12.68%	9.90%

	Maturities	Sinking Fund Requirements December 31, 1980		Sinking Fund Requirements December 31, 1979	
		Cash	Other*	Cash	Other*
	(In Thousands of Dollars)				
1980	—	—	—	861	16,992
1981	121,473	681	17,912	861	17,912
1982	38,137	32,573	17,162	32,807	16,662
1983	72,007	40,683	16,946	40,833	16,446
1984	142,660	48,753	16,071	48,903	15,571
1985	692,133	54,988	15,831		

Sinking fund requirements may be met by certification of property additions at the rate of 167% of the required amount.

The outstanding First Mortgage Bonds of the Company's subsidiaries as of December 31, 1980 and 1979 were:

Maturity	2⅞% to 5⅞%	6% to 8⅞%	9% to 11⅞%	12% to 16⅛%	TOTAL
	(In Thousands of Dollars)				
1980					
1981	8,000	—	110,000	—	118,000
1982	15,464	—	—	—	15,464
1983	19,172	—	50,000	—	69,172
1984	31,500	—	—	—	31,500
1985	18,000	—	—	—	18,000
1986 - 1995	182,955	—	526,440	120,000	829,395
1996 - 2005	166,250	511,120	302,050	98,500	1,077,920
2006 - 2010	—	40,000	285,000	55,000	380,000
Total First Mortgage Bonds					2,539,451
1979					
1980	23,400	—	—	—	23,400
1981	8,000	—	110,000	—	118,000
1982	15,572	—	—	—	15,572
1983	19,202	—	50,000	—	69,202
1984	31,500	—	—	—	31,500
1985 - 1994	154,598	—	528,050		682,648
1995 - 2004	211,250	511,160	237,100	—	959,710
2005 - 2009	—	40,000	350,000	55,000	445,000
Total First Mortgage Bonds					2,345,032

NOTE 8. RETAINED EARNINGS

The indenture provisions relating to the operating subsidiaries' long-term debt and transfers by such subsidiaries from retained earnings to the stated value of common stock and the provisions of the MSE bank loan agreement and indenture restrict the amount of consolidated retained earnings available for cash dividends on common stock. As of December 31, 1980, $214,348,000 of consolidated retained earnings were free from such restrictions.

NOTE 9. COMMITMENTS AND FINANCING

The Middle South Sytem's construction program contemplates construction expenditures (including AFDC) of $897 million in 1981, $836 million in 1982 and $704 million in 1983, of which expenditures in the estimated amounts of $207 million, $234 million and $228 million are applicable to MSE's 87.52% interest in the Grand Gulf Plant, a two-unit nuclear generating station. MSE currently projects commercial operation dates of 1982 and 1986 for the first and second units of this plant, respectively. In connection with this plant, the Company has undertaken to furnish or cause to be furnished to MSE, to the extent not obtained by MSE from other sources, sufficient capital for construction and operation of the plant and related purposes. At December 31, 1980, MSE had outstanding intermediate-term revolving credit borrowings and first mortgage bonds in the amount of $1.17 billion and the Company had invested $443.6 million in the common stock of MSE. In the event that Unit No. 1 of the Grand Gulf Plant is not in commercial operation by December 31, 1982, or Unit No. 2 in commercial operation by December 31, 1986, the outstanding bonds and bank borrowings would become due and payable unless extensions of time are arranged. In this case, the Company would be required to provide MSE with sufficient funds, to the extent not obtained by MSE from other sources, to meet these obligations.

The Middle South System Operating Companies are obligated under agreements with MSE to make payments or subordinated advances adequate to cover all of the operating expenses and capital costs of MSE and, in return, are entitled to receive the power available to MSE from the Grand Gulf Plant. During 1980 the operating companies agreed in principle to a permanent allocation of the Grand Gulf Plant's capability. Under this arrangement, those companies receiving allocations, LP&L, MP&L and NOPSI, will assume, in proportion to such allocations, all responsibilities and obligations related to the Grand Gulf Plant and AP&L and Ark-Mo, which did not receive allocations, will relinquish their rights in the plant. These new agreements are subject to receipt of the approval of regulatory agencies and of all other necessary approvals.

The Federal income tax returns for the years 1971 through 1976 have been examined by the Internal Revenue Service (IRS) and adjustments have been proposed. The principal issue is whether customer deposits are includible in taxable income. A formal written protest has been filed and conferences are being held with an Appeals Officer of the IRS. Any final liability for taxes resulting from settlement with the IRS would not have a material effect on net income. Income taxes on customer deposits would be normalized. Most of the other issues have been settled and adequate provisions have been recorded.

SFI has a long-term oil supply agreement with a major oil company providing for the purchase by SFI of 50,000 barrels of oil per day for a twenty year period ending in 1996 with the option, upon two years written notice, to reduce the contract quantity to no less than 35,000 barrels. SFI also has an agreement with another major oil company providing for the purchase by SFI of up to 200,000 barrels of oil per month through 1984.

SFI has contracted with a joint venture for a supply of coal from a mine to be developed in Wyoming which is expected to provide 150 to 210 million tons over a period of twenty-six to forty-two years. AP&L is currently purchasing coal under an agreement that will provide approximately 100 million tons of coal over a twenty year period.

Under the terms of their nuclear fuel leases, three subsidiaries are responsible for the disposal of spent nuclear fuel. These companies consider all costs incurred or to be incurred in the use and disposal of nuclear fuel to be proper components of nuclear fuel expense and provisions to recover such costs have been or will be made in applications to regulatory commissions. AP&L, the only System company with an operating nuclear station, collected approximately $7,382,000 in 1980 for the storage or disposal of spent fuel. AP&L is also recovering approximately $61 million for decommissioning costs for its two nuclear units through increased depreciation charges over the life of the station. Based on an AP&L study, decommissioning costs are projected to be in excess of the amounts currently being collected. AP&L is requesting and will request recovery of these estimated increased costs in applications to its regulatory commissions.

NOTE 10. LEASES

The Company's subsidiaries account for leases on the same basis as that used by their respective regulatory authorities in the ratemaking process which determines the revenues utilized to recover the lease costs.

Application of criteria used to define a capital lease would permit recording the following assets and liabilities on the balance sheet:

	1980	1979	1978
	(In Thousands)		
Assets:			
Utility plant	$ 63,304	$ 61,319	$ 55,722
Accumulated amortization	(16,892)	(16,493)	(12,904)
Net	$ 46,412	$ 44,826	$ 42,818
Other property and investments - net	$ 47,885	$ 50,318	$ 52,751
Liabilities:			
Non-current obligations under capital leases	$104,136	$104,357	$102,293
Current obligations under capital leases	$ 4,588	$ 4,565	$ 3,632

The recording of such leases would not materially affect the amounts reported as either expense or net income.

At December 31, 1980, the companies had noncancellable leases with minimum rental commitments as follows:

	(In Thousands)
1981	$ 36,515
1982	34,163
1983	32,548
1984	29,74[illegible]
1985	28,366
For years thereafter	379,787
	$541,121

Rental expense amounted to approximately $34,441,000, $29,453,000 and $26,977,000 in 1980, 1979 and 1978, respectively.

Three subsidiaries have entered into nuclear fuel leases aggregating $270,000,000. The leases, unless terminated sooner by one of the parties, will continue through 2018, 2028 and 2029. Lease payments, which are not included in the tabulations above, are based on nuclear fuel use. Nuclear fuel lease expense of $37,300,000, $14,998,000 and $13,279,000 was charged to operations in 1980, 1979 and 1978, respectively. The unrecovered cost base of the leases was $238,351,000, $170,989,000 and $103,018,000 at December 31, 1980, 1979 and 1978, respectively.

NOTE 11. PENSION PLANS

Total pension expense of the Company and its subsidiaries for 1980, 1979 and 1978 was $21,253,000, $18,605,000 and $16,843,000, respectively, which includes amortization of past service cost over periods of ten to thirty years. A comparison of accumulated plan benefits and plan net assets for the defined benefit plans is presented below:

	January 1,	
	1980	1979
Actuarial present value of accumulated plan benefits:		
Vested	$217,899	$187,230
Nonvested	14,970	15,189
Total	$232,869	$202,419
Net assets available for plan benefits	$254,784	$221,752

The weighted average assumed rate of return used in determining the actuarial present values of accumulated plan benefits ranged from 6% to 7% for 1980 and 1979.

NOTE 12. QUARTERLY RESULTS (UNAUDITED)

Consolidated operating results for the four quarters of 1980 and 1979 were as follows:

Quarter Ended	Operating Revenues	Operating Income	Net Income	Earnings Per Share
	(In Thousands of Dollars)			
1980:				
March	502,020	61,392	48,144	$0.53
June	486,177	51,427	20,838	$0.22
September	761,874	111,968	83,816	$0.85
December	582,157	73,035	43,109	$0.41
1979:				
March	401,579	58,899	50,247	$0.60
June	407,257	43,556	34,131	$0.40
September	558,121	70,764	61,777	$0.73
December	476,102	44,979	35,903	$0.40

The business of the Middle South System is subject to seasonal fluctuations with the peak period occurring during the summer months. Accordingly, earnings information for any three month period should not be considered as a basis for estimating results of operations for a full year.

NOTE 13. OIL AND GAS RESERVES (UNAUDITED)

Financial Accounting Standards Board (FASB) Statement No. 19, as amended by Statement No. 25, requires disclosure of certain information pertaining to oil and gas reserves. SFI serves the Middle South System on a non-profit basis and is limited in its recovery to the cost of such reserves. Billings to System companies are based upon a unit-of-production cost, determined on the basis of proved developed reserves, as defined by FASB Statement No. 25. The following table sets forth information as to the estimated net quantities of reserves, all of which are located within the United States, as of the dates indicated:

	1980	
	Natural Gas (MCF)	Oil and Condensate (Barrels)
Proved developed reserves:		
As of January 1, 1980	73,167,069	1,858,523
Revisions of previous estimates	(13,702,714)	(362,763)
Extensions, discoveries, and other additions	3,862,680	472,798
Production	(5,506,657)	(228,672)
As of December 31, 1980	57,820,378	1,739,886
Proved undeveloped reserves as of December 31, 1980	800,722	359,628
Proved developed and undeveloped reserves as of December 31, 1980	58,621,100	2,099,514

	1979	
	Natural Gas (MCF)	Oil and Condensate (Barrels)
Proved developed reserves:		
As of January 1, 1979	94,887,410	1,224,629
Revisions of previous estimates	(18,023,557)	(298,139)
Extensions, discoveries and other additions	3,244,252	1,060,453
Production	(5,069,375)	(107,942)
Sale of minerals in place	(1,871,661)	(20,478)
As of December 31, 1979	73,167,069	1,858,523

Information with respect to proved undeveloped reserves is only available as of December 31, 1980.

NOTE 14. EFFECT OF INFLATION ON OPERATIONS (UNAUDITED)

The following supplementary information about the effects of changing prices on the Company is provided in accordance with the requirements of Statement of Financial Accounting Standards No. 33, "Financial Reporting and Changing Prices". It should be viewed as an estimate of the effect of changing prices, rather than as a precise measure.

Statement of Income from Operations and Other Financial Data
Adjusted for Effects of Changing Prices for the Year ended December 31, 1980
(In Thousands)

	As Reported in the Financial Statements	Adjusted for General Inflation (Constant Dollars)	Adjusted for Changes in Specific Prices (Current Costs)
Revenues[1]	$2,342,228	$2,342,228	$2,342,228
Operating expenses (excluding depreciation)[1]	1,902,409	1,902,409	1,902,409
Depreciation	141,997	285,262	320,105
Total operating expenses	2,044,406	2,187,671	2,222,514
Operating income	297,822	154,557	119,714
Other income[1]	235,580	235,580	235,580
Interest & other charges[1]	337,495	337,495	337,495
Income from operations (excluding reduction to net recoverable cost)[2]	$ 195,907	$ 52,642	$ 17,799
Increase in specific prices (current costs) of property, plant and equipment held during the year[3]			$1,660,089
Reduction to net recoverable cost		$ (571,075)	(905,432)
Effect of increase in general price level			(1,222,213)
Excess of increase in general price level over increase in specific prices after reduction to net recoverable cost			(467,556)
Gain from decline in purchasing power of net amounts owed		225,345	225,345
Net		$ (345,730)	$ (242,211)

[1]*Assumed to be in "average for the year" dollars and thus are not restated.*
[2]*Including the reduction to net recoverable cost, the loss from operations on a constant dollar basis would have been $518,433 for 1980.*
[3]*At December 31, 1980 current cost of property, plant and equipment, net of accumulated depreciation, was $11,654,904, while historical cost or net cost recoverable through depreciation was $6,629,111.*

Five-Year Comparison of Selected Supplementary Financial Data
Adjusted for Effects of Changing Prices
In Thousands of Average 1980 Dollars

	1980	1979	1978	1977	1976
OPERATING REVENUES	$2,342,228	$2,069,600	$2,048,891	$1,962,239	$1,656,543
HISTORICAL COST INFORMATION ADJUSTED FOR GENERAL INFLATION					
Income from operations (excluding reduction to net recoverable cost)	$ 52,642	$ 74,049			
Income per common share (after dividend requirements on preferred stock and excluding reduction to net recoverable cost)	$0.54	$0.86			
Net assts at year-end at net recoverable cost	$1,819,986	$1,790,279			
CURRENT COST INFORMATION					
Income from operations (excluding reduction to net recoverable cost)	$ 17,799	$ 41,503			
Income per common share (after dividend requirements on preferred stock and excluding reduction to net recoverable cost)	$0.18	$0.49			
Excess of increase in general price level over increase in specific prices after reduction to net recoverable cost	$ 467,556	$ 590,976			
Net assets at year-end at net recoverable cost	$1,819,986	$1,790,273			
GENERAL INFORMATION					
Gain from decline in purchasing power of net amounts owed	$ 225,345	$ 309,324			
Cash dividends declared per common share	$1.59	$1.74	$2.05	$2.27	$2.46
Market price per common share at year-end	11½	13⅝	18⅜	22	23⅞
Average consumer price index	246.8	217.4	195.4	181.5	170.5

NOTE: The Statement requires that historical cost information adjusted for general inflation and current cost information be provided for 1979 and subsequent years. Comparable information is not readily available for the years prior to 1979 and thus is not provided.

Constant dollar amounts represent historical costs adjusted for the effects of general inflation. The effects are determined by converting these costs into dollars of equal purchasing power using the Consumer Price Index for all Urban Consumers (CPI-U).

Current cost amounts reflect the changes in specific prices of property, plant and equipment from the year of acquisition to the present. The current costs of property, plant and equipment, which represent the estimated costs of replacing existing plant assets, are determined by applying the Handy-Whitman Index of Public Utility Construction Costs (HWI) to the cost of the surviving plant by year of acquisition. Land and certain other plant assets which are not included in the HWI were converted using the CPI-U. The difference between current cost amounts and constant dollar amounts results from specific prices of property, plant and equipment (as measured by the Handy-Whitman Index) changing at a rate different than the rate of general inflation (as measured by the Consumer Price Index).

The current year's depreciation expense on the constant dollar and current cost balances of property, plant and equipment were determined by applying the Company's depreciation rates to the indexed amounts.

Fuel inventories, the cost of fuel used in generation, and gas purchased for resale have not been restated from their historical cost in nominal dollars. Regulation limits the recovery of fuel and purchased gas costs 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 of Financial Accounting Standards No. 33, income taxes were not adjusted.

The regulatory commissions to which the Company's subsidiaries are subject allow only the historical cost of plant to be recovered in revenues as depreciation. Therefore, the excess cost of plant stated in terms of constant dollars or current cost over the historical cost of plant is not presently recoverable in rates. This excess 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, the Company believes, based on past experiences, that 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 Income from Operations presented above, the reduction of net property, plant and equipment to net recoverable cost is 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.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

I. FINANCIAL CONDITION

In recent years the Middle South System has experienced financial problems resulting primarily from the System's massive construction program made necessary by customer requirements and the need to diversify the System's fuel base. The increasing cost of construction and the ever-lengthening construction periods have further aggravated this situation. At the end of 1980, the amount invested in construction work-in-progress (CWIP) was $3.2 billion, an increase of $2.0 billion over the amount invested at the end of 1976. Financing this investment has been a significant task in itself, but the reluctance of regulatory bodies to provide adequate rate relief and to allow the System operating companies current recovery of the carrying cost of CWIP has made the task even more difficult.

Reported earnings rose approximately $10 million from 1978 to 1980, while earnings exclusive of the effect of capitalizing the carrying cost of CWIP, Allowance for Funds Used During Construction (AFDC), declined $81 million. This decline resulted primarily from the increase in the amount and cost of debt and preferred stock that the System has outstanding, the major portion of which was issued to finance CWIP, and the effect of inflation on the System's operating expenses. Generally, fuel cost increases are recovered currently through fuel adjustment clauses. Increases in other operating expenses, however, can only be recovered through the regulatory process during which costs continue to rise and earnings decline further.

The delay in recovering these costs reduced internally generated funds available for construction and at the same time reduced the System operating companies' mortgage bond and preferred stock earnings coverage ratios to the point where conventional sources of external financing, mortgage bonds and preferred stock, were severely limited. To keep the System financially viable, a program was instituted to conserve cash flow. This program was implemented through delays in construction programs and the initiation of an austerity policy throughout the System. In addition, in order to continue construction, the System continued to use non-conventional financings such as sale and leaseback arrangements and sales of plant under construction to third parties. In one case, as discussed further below, an operating company temporarily ceased supplying funds for the construction of certain generating units.

At the end of 1980, however, based on increased rates approved in 1979, pending rate increase applications and rates implemented in 1980 but subject to refund, the Company hopes that increased funds will be available for the System's scheduled construction program. The detrimental effect that the large CWIP balance has on cash flow will only be alleviated when the utility plant involved is placed in service or the regulatory bodies allow a cash return on CWIP.

II. LIQUIDITY AND CAPITAL RESOURCES

During the period 1978 to 1980 the Middle South System had construction expenditures of $2.8 billion, including AFDC, of which over 80 percent was funded by external financing. Projected construction expenditures for 1981 through 1983 are $2.4 billion which is estimated to be funded in large part through external sources but to a lesser extent than in recent years.

Due to the earnings coverage ratio constraints on the System operating companies during the last three years, conventional sources of financing for construction had to be supplemented with non-conventional sources, primarily sale and leaseback arrangements. Although $80.6 million was raised from these sources during that period, they are expected to contribute a lesser amount in the future. During 1980 one operating company exercised its option and temporarily ceased supplying its portion of funds for the construction of three jointly-owned coal units. Construction was not interrupted, however, as one of the co-owners agreed, as provided in the related ownership agreement, to advance the operating company's share of construction funds. This advance, amounting to approximately $69 million through 1980, is scheduled for repayment in 1981.

Given improved earnings levels in late 1980 and assuming the receipt of timely and adequate rate relief in response to pending rate increase applications, the System operating companies' mortgage bond and preferred stock earnings coverage ratios should permit greater use of conventional financing methods for their construction requirements. In addition, AP&L, LP&L, MP&L and NOPSI are currently authorized to make short-term borrowings in an aggregate amount outstanding at any one time of up to the lesser of $427 million or 10 percent of capitalization. At December 31, 1980, only $81 million of short-term borrowings were outstanding compared to $113 million at December 31, 1979. These companies had available unused lines of credit of $296 million.

Middle South Energy (MSE), the only non-operating company with a significant construction program, contemplates construction expenditures for 1981 through 1983 of $669 million, including AFDC, for its portion of the costs of building the Grand Gulf Plant, a two-unit nuclear generating station. The first unit is scheduled for commercial operation in 1982 and the second in 1986. In connection with this Plant, the Company has undertaken to provide or cause to be provided to MSE sufficient capital to complete the Plant. To this end, through 1980 the Company had invested $443.6

million in MSE's common stock. In addition, MSE had sold an aggregate of $498.5 million of its first mortgage bonds and had arrangements with a group of banks under an intermediate-term revolving credit agreement to borrow up to $808 million. At year-end 1980, $137 million of MSE's revolving credit line remained unused. In order to obtain additional funds required to complete Unit No. 1, MSE is negotiating for an increase in its revolving credit line up to $1.3 billion. MSE has covenanted to complete Unit No. 1 by the end of 1982 and to complete Unit No. 2 by the end of 1986. If either of these covenants were not fulfilled, the outstanding bonds and bank borrowings would then become due and payable, unless extensions could be arranged, and the Company would be required to provide MSE with sufficient funds to meet these obligations to the extent not provided from other sources. MSE is also negotiating for changes in these covenants to extend the dates by which Unit Nos. 1 and 2 must be completed to not later than December 31, 1984, and December 31, 1988, respectively.

In order to maintain an acceptable capital structure and to provide the System operating companies and MSE with additional funds to continue their construction programs, the Company must maintain its ability to market its common stock. During the period 1978 to 1980, the Company issued an aggregate of 40,141,333 shares of common stock, providing the Company with net cash proceeds of approximately $548 million. These funds were utilized to repay revolving credit borrowings incurred to purchase additional common stocks of the Company's subsidiaries. The Company's existing revolving credit agreement provides for borrowings of up to $230 million, of which approximately $121 million remained unused at year-end 1980.

In addition to obtaining funds for its construction program, the Middle South System will need to raise during the period of 1981 through 1983 $315 million to meet debt maturities and cash sinking funds and to make preferred stock sinking fund redemptions. It is anticipated that a substantial portion of these requirements will be funded through external sources, including the sales of similar securities, and that the balance will be provided by internally generated funds.

III. RESULTS OF OPERATIONS

After a decline in 1979, net income increased slightly in 1980. While net income is the result of many factors, there are several that had a significant effect on the System's results of operations for these years.

Increased electric operating revenues each year were largely due to increased fuel-related costs which were billed to customers, as allowed by the fuel adjustment clauses, but which also appeared as offsetting increases to operating expenses, resulting in no contribution to net income. Although approximately $200 million of rate increases were granted to the System operating companies by their regulatory bodies over the last three years, this relief was neither timely nor sufficient to cover the rising costs of operations associated with the double-digit inflation that our nation has experienced. At year-end 1980, the System had outstanding rate increase applications totalling approximately $465 million, of which $19 million was collected subject to refund during the year. Increases in energy sales contributed less to net income than in earlier years averaging less than 6 percent per year during these three years.

The small increase in gas operating revenues resulted from a lower volume of sales, a trend caused by conservation efforts of gas customers, offset by increased gas cost recoveries.

Carrying charges associated with construction, AFDC, were capitalized. Since these charges were not expensed during the current period, net income during this period was substantially increased. The amount reported as AFDC represents the costs of funds invested by common and preferred stockholders plus the after-tax cost of borrowed funds that were used to finance the construction program. These credits to the income statement are intended to remove the effect of the costs of financing the construction of new facilities from net income; they do not provide any current cash to the System. AFDC was 80 percent, 117 percent and 122 percent of net income for 1978, 1979 and 1980, respectively.

The substantial increases in interest and preferred dividend requirements during the last three years reflected additional issuances of debt and preferred stock, the proceeds of which were applied to finance construction, and the very significant increases in prevailing interest and preferred dividend rates.

IV. EFFECT OF INFLATION

Inflation has had a significant impact on the Company's operations in recent years. (See Note 14 to the Consolidated Financial Statements - "Effect of Inflation on Operations.")

V. SUMMARY

The ability of the Middle South System to reach and maintain a sound financial position while providing the generating capacity necessary to serve the present and future energy demands of its customers at reasonable costs depends primarily on timely, fair and sufficient rate relief from the System's regulatory bodies.

1970-1980 FINANCIAL RECORD (in thousands)

CONSOLIDATED SUMMARY OF OPERATIONS

	1980	1979	1978
Operating Revenues:			
Electric	$ 2,181,320	$1,669,451	$1,489,915
Natural gas	116,796	116,612	95,863
Transit	44,112	36,996	36,399
Total	2,342,228	1,823,059	1,622,177
Operating Expenses:			
Operation:			
Fuel for electric generation	946,145	697,606	623,402
Purchased power	281,951	258,377	133,929
Gas purchased for resale	88,864	88,801	68,657
Other	283,905	200,264	199,406
Maintenance	111,[illegible]31	111,394	99,941
Depreciation	141,997	119,304	112,805
Taxes other than income taxes	84,690	77,849	69,771
Income taxes	105,023	51,266	86,004
Total	2,044,406	1,604,861	1,393,915
Operating Income	297,822	218,198	228,262
Other Income:			
Allowance for equity funds used during construction	122,277	124,086	93,573
Miscellaneous income and deductions — net	7,019	7,940	6,239
Income taxes — cr.	106,284	76,232	50,105
Total	235,580	208,258	149,917
Interest and Other Charges:			
Interest on long-term debt	327,468	255,242	199,212
Other interest-net	72,666	42,139	22,769
Allowance for borrowed funds used during construction — (cr.)	(117,663)	(89,247)	(54,717)
Preferred dividend requirements of subsidiaries	55,024	36,264	25,477
Minority interest in subsidiary's net income	—	—	—
Total	337,495	244,398	192,741
Net Income	$ 195,907	$ 182,058	$ 185,438
Earnings Per Share (based on average number of shares outstanding)	$2.01	$2.13	$2.46
Dividends Declared Per Share	$1.59	$1.535	$1.46
Average Number of Common Shares Outstanding ($5 Par Value)	97,469,169	85,444,691	75,522,179

UTILITY PLANT AND CAPITALIZATION DATA (at December 31)

	1980	1979	1978
Fixed Assets:			
Utility Plant	$ 7,893,636	$7,002,052	$6,052,023
Less accumulated depreciation and amortization	1,264,525	1,139,164	1,038,256
Utility plant-net	$ 6,629,111	$5,862,888	$5,013,767
Capitalization:			
Long-term debt	$ 3,392,309	$3,017,816	$2,629,711
Preferred stock (including premium and issuance expense):			
Without sinking fund	330,967	330,966	280,712
With sinking fund	283,1[illegible]5	193,508	60,063
Common equity	1,905,5[illegible]	1,664,060	1,415,239
Minority interest in the common equity of Arkansas-Missouri Power Company	—	—	—
Total	$ 5,911,969	$5,206,350	$4,385,725
Capitalization Ratios:			
Long-term debt	57.4%	58.0%	60.0%
Preferred stock (including premium and issuance expense)	10.4	10.1	7.8
Common equity	32.2	31.9	32.2

Certain amounts have been restated for comparative purposes and to reflect ratemaking decisions affecting prior years.

1977	1976	1975	1974	1973	1972	1971	1970
$1,327,319	$1,063,036	$ 868,100	$ 768,297	$ 609,082	$ 550,089	$ 473,352	$ 420,937
83,910	62,502	49,513	38,409	38,362	31,884	21,267	17,885
31,828	18,873	13,176	11,091	10,933	11,408	11,646	11,668
1,443,057	1,144,411	930,789	817,797	658,377	593,381	506,265	450,490
568,990	422,204	294,482	250,435	149,882	120,940	92,409	76,672
86,087	61,439	35,075	43,880	22,458	18,705	12,351	5,315
58,577	37,852	30,994	21,807	19,936	18,774	11,747	7,995
180,887	145,489	139,708	116,486	107,776	102,968	92,192	84,232
72,708	58,694	50,729	46,662	40,776	36,893	31,540	29,391
106,748	101,045	92,770	74,635	68,781	64,439	58,132	52,926
67,306	61,561	56,481	49,127	49,224	46,068	42,363	39,211
98,091	68,795	55,560	31,632	52,957	52,801	53,582	54,504
1,239,394	957,079	755,799	643,664	511,790	461,588	394,316	350,246
203,663	187,332	174,990	174,133	146,587	131,793	111,949	100,244
65,346	62,169	46,064	49,509	31,948	22,188	14,628	10,080
6,910	8,329	4,397	2,885	2,421	913	590	1,485
29,393	18,287	14,175	(1,788)	(1,069)	(455)	(304)	(801)
101,649	88,785	64,636	50,606	33,300	22,646	14,914	10,764
153,005	132,719	113,486	105,532	72,464	61,110	50,662	40,209
18,260	15,571	19,177	8,094	3,723	2,870	1,553	2,726
(34,031)	—	—	—	—	—	—	—
23,109	21,780	16,660	15,040	13,181	10,642	8,833	7,287
—	—	—	—	—	46	18	—
160,343	170,070	149,323	128,666	89,368	74,668	61,066	50,222
$ 144,969	$ 106,047	$ 90,303	$ 96,073	$ 90,519	$ 79,771	$ 65,797	$ 60,786
$2.18	$1.82	$1.78	$2.17	$2.09	$1.98	$1.68	$1.61
$1.395	$1.335	$1.275	$1.23	$1.15	$1.07	$1.03	$0.975
66,598,876	58,395,628	50,733,782	44,279,481	43,376,255	40,25[illegible]53	39,213,614	37,687,885
$5,183,284	$4,539,891	$3,953,814	$3,470,598	$3,054,867	$2,672,464	$2,386,077	$2,059,387
935,702	831,930	747,612	668,148	608,613	546,378	502,740	436,579
$4,247,582	$3,707,961	$3,206,202	$2,802,450	$2,446,254	$2,126,086	$1,883,337	$1,622,808
$2,175,471	$1,965,985	$1,751,328	$1,529,958	$1,341,637	$1,147,127	$ 983,941	$ 829,053
280,712	250,679	240,627	240,627	230,611	205,558	160,431	150,369
60,063	60,063	60,063	—	—	—	—	—
1,197,807	1,010,278	864,035	746,628	705,212	576,262	538,935	494,504
—	—	—	—	—	—	637	—
$3,714,053	$3,287,005	$2,916,053	$2,517,213	$2,277,460	$1,928,947	$1,683,944	$1,473,946
58.6%	59.8%	60.1%	60.8%	58.9%	59.5%	58.5%	56.3%
9.2	9.5	10.3	9.5	10.1	10.6	9.5	10.2
32.2	30.7	29.6	29.7	31.0	29.9	32.0	33.5

CORPORATE OBJECTIVES In fulfilling our public trust as a corporate citizen, Middle South Utilities is firmly committed to these primary objectives:

1. To furnish reliable utility services to customers at the lowest reasonable cost consistent with sound business practices, while continuing to respond to their needs in a courteous and efficient manner.

2. To attain the financial integrity necessary for System companies to provide a fair return to stockholders and to continue serving their customers effectively. Emphasis will be on optimizing capitalization ratios and earning a fair return on capital, including that invested in construction, with resultant improved coverages, internal cash generation, and quality of earnings.

3. To seek continual improvement of the work environment within the System to increase productivity, promote safe and efficient operations, encourage employee growth and development, and minimize employee turnover.

4. To be a socially responsible corporate citizen by emphasizing such activities as the social and economic development of our service area and the continuing practice of sound environmental policies consistent with sound business practices.

5. To encourage the efficient use of energy through such practices as conservation and load management, and to promote the development and application of innovative energy technology and renewable resources when it is economic to the customer and provides a fair return on investment.

STOCKHOLDER GROWTH. At the close of 1980, MSU had 175,326 stockholders, or 31,258 more than a year earlier. The number of shares of common stock outstanding increased from 90,432,998 at the end of 1979 to 107,349,943 as of December 31, 1980.

DIVIDEND REINVESTMENT AND STOCK PURCHASE PLAN. The Company's Dividend Reinvestment and Stock Purchase Plan became a more attractive option when, effective with the July 1, 1980, dividend, a five-percent discount feature was added. Under the plan, dividend payments are used to buy additional shares of MSU common stock. Cash purchases of additional shares may also be made by plan participants. No commission or service charge is paid by participating stockholders in connection with purchases under the plan. Information about participation in the plan can be secured by writing Dan E. Stapp, secretary of the Company.

DIVIDENDS. Dividends of $1.58 per share were paid on Middle South common stock in 1980. This was up from the 1979 rate of $1.52 per share.

An estimated 98.24 percent of the dividends paid in 1980 are nontaxable as dividend income to the stockholder. This is mainly due to the fact that a large portion of reported net income which resulted from capitalizing the costs of the capital invested in projects still under construction does not constitute taxable income.

Donald J. Winfield,
senior vice president

This nontaxable portion of dividends is treated, for income tax purposes, as a return of the stockholder's capital. When the stockholder ultimately sells or otherwise disposes of shares, this return of capital should be deducted from the tax cost of the shares in computing gain or loss for income tax purposes.

The five-percent discount applicable to the purchase of shares through the Dividend Reinvestment and Stock Purchase Plan is considered, for federal income tax purposes, to be an additional distribution and is treated the same as dividends paid.

The quarterly dividend paid on January 2, 1981, reflected a one-cent increase to 40½¢ per share. This is equivalent to an annual rate of $1.62 per share. With the single exception of 1956, the Company has been able to increase the dividend every year since its organization.

ORGANIZATIONAL AND MANAGEMENT CHANGES. The previously announced plan to consolidate Ark-Mo and AP&L became effective January 1, 1981. In this consolidation of operations, Ark-Mo became a division of AP&L. Associated Natural Gas Company, formerly an Ark-Mo subsidiary, became a subsidiary of AP&L.

Donald J. Winfield, senior vice president of MSU, will retire on March 31, 1981, after almost 25 years with the Company.

On May 16, 1980, Frank G. Smith, Jr., president of Ark-Mo, became president and chief executive officer of MSS, succeeding F. E. Autrey, who resigned as president of MSS and MSU. Floyd W. Lewis, then chairman and chief executive officer of MSU and MSS, assumed the MSU presidency vacated by Autrey.

MIDDLE SOUTH UTILITIES, INC., an investor-owned public utility holding company, owns 100 percent of the common stock of four operating companies — Arkansas Power & Light Company, Louisiana Power & Light Company, Mississippi Power & Light Company, and New Orleans Public Service Inc. The two other principal subsidiaries of the Company are Middle South Services, Inc., a service company, and Middle South Energy, Inc., which owns the major portion of Grand Gulf Nuclear Station, a 2.5-million-kilowatt generating facility now under construction in Mississippi.

System Fuels, Inc., is a fuels procurement subsidiary of the four operating companies. Associated Natural Gas Company is a gas distribution subsidiary of Arkansas Power & Light Company.

With Middle South Utilities, Inc., these companies constitute the Middle South Utilities System.

SALES IN KILOWATT-HOURS (thousands)

	Total	Residential	Commercial	Industrial	Other
1980	**55,154,237**	**16,065,362**	**9,276,714**	**22,876,339**	**6,935,822**
1979	52,946,799	14,606,178	8,754,087	22,329,201	7,257,333
1978	51,973,705	14,781,680	8,635,615	19,714,164	8,842,246
1977	48,477,281	13,852,810	7,972,364	18,712,127	7,939,980
1976	42,957,761	12,232,611	7,240,843	16,831,622	6,652,685
1975	38,742,993	11,942,436	6,906,944	13,619,710	6,273,903
1974	37,779,407	11,012,164	6,370,308	14,965,405	5,431,530
1973	37,862,524	11,261,040	6,364,193	14,530,792	5,706,499
1972	37,808,576	10,281,403	5,834,029	13,519,543	8,173,601
1971	35,136,681	8,808,078	5,214,614	12,029,426	9,084,563
1970	32,531,614	8,005,340	4,761,833	11,267,636	8,496,805

REVENUE FROM ELECTRIC ENERGY SALES (thousands)

	Total	Residential	Commercial	Industrial	Other
1980	**$2,139,327**	**$738,073**	**$447,688**	**$721,378**	**$262,188**
1979	1,659,192	553,746	357,064	529,008	219,374
1978	1,479,759	505,790	317,412	408,319	248,238
1977	1,328,983	466,299	291,807	369,405	201,472
1976	1,051,270	373,631	243,480	290,558	143,601
1975	856,009	325,944	199,050	209,506	121,509
1974	766,541	289,776	174,553	214,327	87,885
1973	602,842	237,990	141,969	157,173	65,710
1972	543,221	206,086	120,853	131,318	84,964
1971	467,548	174,859	105,795	110,172	76,722
1970	415,543	158,579	96,169	98,476	62,319

RESIDENTIAL CUSTOMERS AND USE

	Average number of customers	Kilowatt-hours per customer	Revenue per customer	Revenue per kilowatt-hour
1980	**1,341,297**	**11,969**	**$549.87**	**4.59¢**
1979	1,314,028	11,116	421.41	3.79
1978	1,280,694	11,542	394.93	3.42
1977	1,238,597	11,184	376.47	3.37
1976	1,208,140	10,125	309.26	3.05
1975	1,182,925	10,[illegible]06	275.54	2.73
1974	1,159,536	9,497	249.91	2.63
1973	1,124,746	10,012	211.59	2.11
1972	1,077,509	9,542	19[illegible].26	2.00
1971	1,014,735	8,680	172.32	1.99
1970	973,621	8,222	162.88	1.98

The common stock of Middle South Utilities, Inc., is listed on the New York, Midwest, and Pacific Stock Exchanges. The stock exchange symbol is MSU. The commonly used abbreviation in stock listings is MidSUt.

ANNUAL MEETING: The Annual Meeting of Stockholders is scheduled to be held in Jackson, Mississippi, at 10:00 AM (CDT), May 15, 1981. The 1980 Annual meeting was held in New Orleans, Louisiana, on May 16, 1980, and 80.3 percent of the shares then outstanding were represented in person or by proxy.

TRANSFER AGENTS: Morgan Guaranty Trust Company of New York, New York 10015; The First National Bank of Boston, Boston 02102; Continental Illinois National Bank and Trust Company of Chicago, Chicago 60690; Hibernia National Bank in New Orleans, New Orleans 70161; Bank of America National Trust and Savings Association, San Francisco 94120.

REGISTRARS: Morgan Guaranty Trust Company of New York, New York 10015; State Street Bank and Trust Company, Boston 02102; The First National Bank of Chicago, Chicago 60670; Whitney National Bank of New Orleans, New Orleans 70160; Wells Fargo Bank N.A., San Francisco 94120.

ADDITIONAL INFORMATION: For persons who desire additional statistical information, a 1980 Financial and Statistical Report is available on request.

THE 1980 ANNUAL REPORT is prepared for the information of stockholders, employees, and other interested persons. *The Company's 1980 Annual Report to the Securities and Exchange Commission on Form 10-K (including financial statements and financial statement schedules) is available to any stockholder upon request without charge. Persons interested in obtaining a copy should write to Dan E. Stapp, Secretary, at the address below:*

MIDDLE SOUTH UTILITIES, INC.
Box 61005
New Orleans, Louisiana 70161
(504) 529-5262

OFFICERS

FLOYD W. LEWIS
Chairman and President
Age 5[illegible]. Joined MSU System in 1949.

EDWIN A. LUPBERGER
Senior Vice President-Chief Financial Officer
Age 44. Joined MSU System in 1979.
Sixteen years' prior utility industry service.

DONALD J. WINFIELD*
Senior Vice President-Financial Consultant

DAN E. STAPP
Secretary
Age 46. Joined MSU System in 1958.

RODNEY J. ESTRADA
Treasurer
Age 43. Joined MSU System in 1965.

E. EUGENE BROWN
Assistant Treasurer
Age 47. Joined MSU System in 1956.

DOROTHY M. ANTOINE
Assistant Secretary
Age 48. Joined MSU System in 1952.

*Retirement: March 31, 1981

DIRECTORS

GEORGE F. BENNETT
President of State Street Investment Corporation and Federal Street Fund, Inc.
Boston, Massachusetts
Compensation and Nominating Committees

JAMES M. CAIN
President and Chief Executive Officer of New Orleans Public Service Inc.
New Orleans, Louisiana

RICHARD W. FREEMAN
Chairman of the Louisiana Coca-Cola Bottling Company, Ltd.; Chairman of the Finance Committee of Delta Air Lines, Inc.
New Orleans, Louisiana
Executive, Audit (Chairman), and Nominating Committees

FLOYD W. LEWIS
Chairman and President of the Company
New Orleans, Louisiana
Executive (Chairman) and Nominating Committees

DONALD C. LUTKEN
President and Chief Executive Officer of Mississippi Power & Light Company
Jackson, Mississippi

JERRY L. MAULDEN
President and Chief Executive Officer of Arkansas Power & Light Company
Little Rock, Arkansas

LeROY P. PERCY
Cotton farmer; Chairman of the Boards of Mississippi Chemical Company and First Mississippi Corporation
Greenville, Mississippi
Executive, Audit, and Nominating (Chairman) Committees

ROBERT D. PUGH
President of Portland Gin Company (Agricultural and Agri-Business) and Chairman of the Board of Directors of Portland Bank
Portland, Arkansas
Executive, Audit, and Nominating Committees

GEORGE K. REEVES
Partner of Ward and Reeves, attorneys
Caruthersville, Missouri
Compensation and Nominating Committees

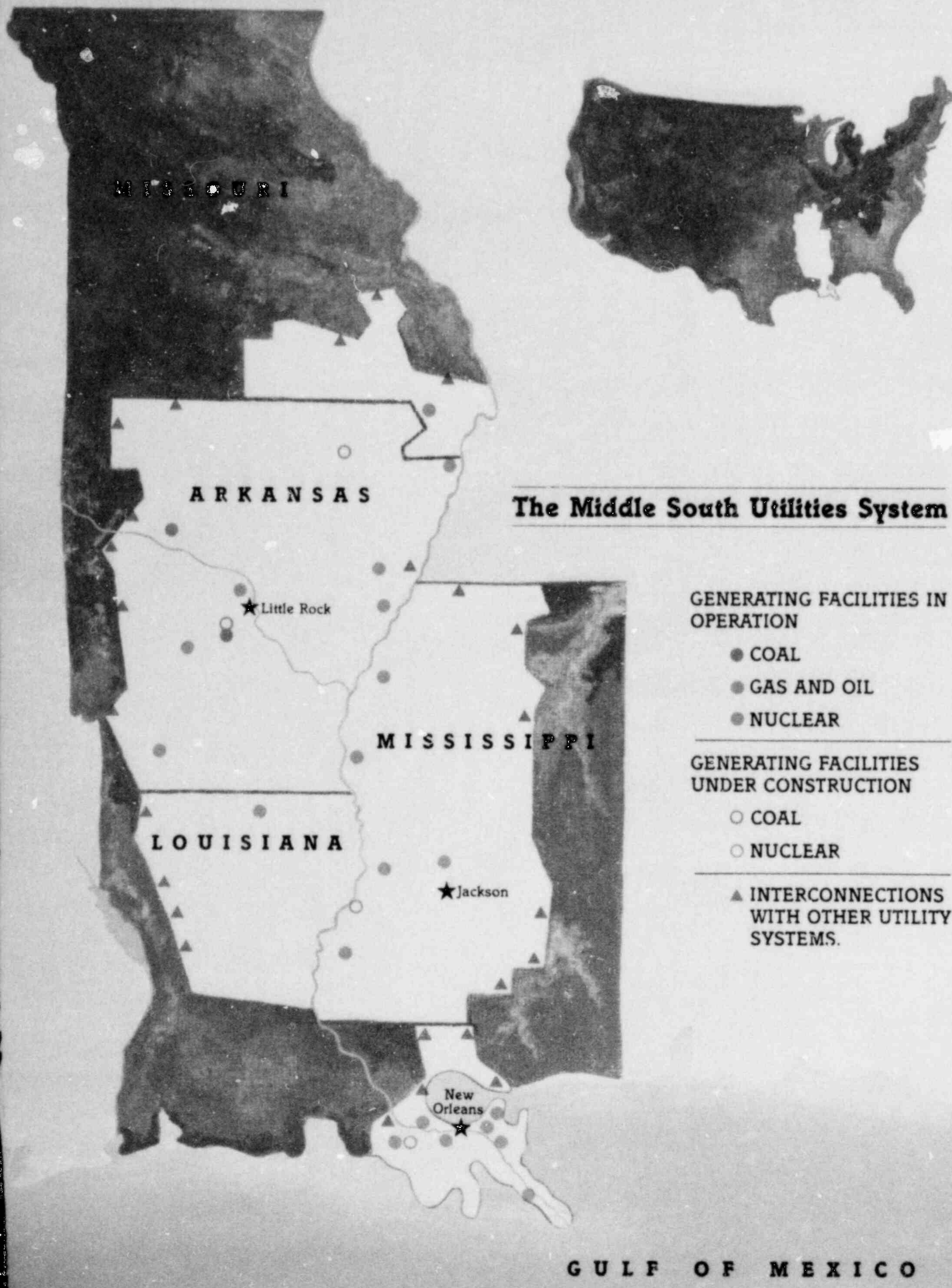
FRANK G. SMITH, JR.
President and Chief Executive Officer of Middle South Services, Inc.
New Orleans, Louisiana

DR. WALTER WASHINGTON
President of Alcorn State University
Lorman, Mississippi
Audit and Nominating Committees

R. E. L. WILSON
Chairman of the Boards of Lee Wilson & Co. (Agricultural and Agri-Business) and The Bank of Wilson.
President of Delta Products Company (Cottonseed Oil Mill)
Wilson, Arkansas
Compensation (Chairman) and Nominating Committees

JACK M. WYATT
President and Chief Executive Officer of Louisiana Power & Light Company
New Orleans, Louisiana
Executive Committee

MIDDLE SOUTH UTILITIES, INC.
Post Office Box 61005
New Orleans, Louisiana 70161


The Middle South Utilities System
MISSOURI
ARKANSAS
Little Rock
MISSISSIPPI
LOUISIANA
Jackson
New Orleans
GULF OF MEXICO
GENERATING FACILITIES IN OPERATION
COAL
GAS AND OIL
NUCLEAR
GENERATING FACILITIES UNDER CONSTRUCTION
COAL
NUCLEAR
INTERCONNECTIONS WITH OTHER UTILITY SYSTEMS.