

“ What actions  
are you taking to  
move the company  
forward? ”

“ Other energy  
companies have  
pulled out of trading  
and marketing.  
Why are you still in? ”

“ With all the  
distractions, can  
you stay focused  
on customers? ”



**FRED J. FOWLER**  
PRESIDENT  
CHIEF OPERATING OFFICER

## WE'RE DRAWING ON OUR CORE STRENGTHS – RELIABILITY, EFFICIENCY AND PRODUCTIVITY.

We're responding to the current industry slump as we have to previous downturns in our industry and the economy – by focusing on productivity and efficiency throughout our operations, and by safely and reliably meeting customers' energy needs. My job as chief operating officer is to make sure that we not only maintain our record of operational excellence – we improve it.

In recent months, we've taken a hard look at costs across the enterprise. We've delayed projects and sold assets, and we're reducing our workforce by nearly 2,000 to reflect current market realities. Many of those moves have involved our competitive merchant energy business, where market conditions present the greatest challenges.

All indicators – excess supply, narrow spark spreads and difficult credit conditions – point to a slow recovery for merchant energy. Our 20 natural gas-fired merchant power plants are under-used in today's oversupplied electricity market. But state-of-the-art technology, leveraged with nearly 100 years of power generation experience, puts our merchant generation fleet among the most efficient and well-run in the U.S. – a competitive advantage when the economy recovers and power demand catches up with supply.

### Our regulated businesses provide stability going forward.

The strong cash flows and steady growth of our regulated businesses will be the bedrock of our earnings for the foreseeable future. Duke Power and Duke Energy Gas Transmission are focused on maximizing profits by increasing productivity and sales.

Duke Power continues to raise the bar for operational excellence. In 2002, the utility's nuclear stations generated more electricity for the Carolinas than ever before – producing at more than 95 percent of their capacity, and at the lowest production cost ever. A higher capacity factor reflects fewer and shorter outages, boosting productivity. We do expect a lower nuclear capacity factor in 2003, as a result of planned maintenance and refueling outages.

The utility's hydroelectric and fossil fleet achieved outstanding commercial availability of 98.3 percent in 2002. Combined with higher nuclear output, that availability helped meet more of the system's power demand at less cost. The fossil/hydro plants met summer peak power demands, thanks to the company's careful management of water resources during the Carolinas' worst drought in 100 years. And through prudent planning, the fleet maintained system reliability while installing the latest environmental technology to reduce emissions at six of the utility's eight coal-fired stations.

Innovation, commitment to customer service and an unwavering focus on safety and reliability have established Duke Energy Gas Transmission as an industry leader, and we are responding to the needs of our customers with new projects and new ideas. Investment in new technologies and advanced preventive maintenance practices are further enhancing the reliability of our pipelines. Capacity in our wholly owned U.S. pipelines is nearly 95 percent contracted with an average contract life of nine years. Union Gas, our distribution company in Ontario, continues to grow, adding more than 20,000 new customers in 2002. This stable customer base and growing demand for reliable sources of natural gas strengthen our earnings base, cash flow and growth potential.

The sharing of expertise, capabilities and market knowledge among our diverse businesses, within regulatory limits, drives efficiencies to boost our bottom line. Here's one example: We use small jet-engine-like turbines for both gas compression in our pipelines and gas-fired electric generation in remote areas around the globe. Operating teams from our gas transmission business in Canada and our generation facilities in Ecuador, France and Australia saw a common interest. They worked out a plan to purchase maintenance services and spare parts for the turbines as a fleet, saving an estimated 20 to 25 percent – millions of dollars – over the life of the equipment.

#### BUYING AND SELLING ENERGY IS AN IMPORTANT PART OF OUR BUSINESS.

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The wholesale energy market is where we buy fuel for our power plants and sell their output. Our sales and marketing activities allow us to buy energy at the lowest possible cost and sell it at the highest fair price, providing higher returns on our investment in merchant plants and other energy infrastructure.

And sales and marketing are critical to the efficient movement of energy in the wholesale marketplace. These activities bring reliable, fair-priced energy to our customers, when and where they need it, along with energy-related products and services.

Most of our market transactions are related to our assets, or conducted on behalf of our customers. We do little proprietary trading, which involves buying and selling energy commodities to profit from price fluctuations. In 2002, only about 10 percent of Duke Energy North America's gross margin was the result of proprietary trading.

Some companies have exited the business, true, but we're seeing new entrants, especially banks and oil companies. We welcome those new market participants, their confidence in this business and the liquidity they bring back to the energy marketplace.

#### CUSTOMERS FACE THEIR OWN CHALLENGES, AND WE OFFER SOLUTIONS.

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Most of our customers are facing the same economic pressures as we are. This presents a real opportunity to build on our business relationships by helping new and existing customers manage their energy needs and costs.

We're reaching for larger market share with wholesale customers, who look to Duke Energy for price risk management and reliable energy supply.

For example, Duke Energy is saving the city of North Little Rock, Ark., a projected \$2.2 million over five years, by reliably supplying its electricity needs at lower cost than competitors could offer. Our cost-efficient generation and marketing capabilities combined to give us that competitive advantage.

On the retail side, Duke Power is ranked #1 for customer satisfaction in the TQS Research survey of large industrial and commercial customers of electric utilities, and consistently ranks first or second with residential customers on the American Customer Satisfaction Index. Awards and surveys that put us at the top of the charts are in the nice-to-know category, but our greatest satisfaction comes from knowing that we're meeting our customers' expectations.

Union Gas has launched a web-based system that enables its business customers to conduct energy transactions online. At Duke Power, we're rolling out mobile meter reading to measure customer usage with pinpoint accuracy, in a fraction of the time and at less cost than manual reading.

When a December 2002 ice storm in the Carolinas left nearly 1.4 million customers in the cold and the dark, Duke Power restored service to more than 150,000 customers per day – more than ever before. This dramatic restoration rate drew on our experience in previous storms: Following the devastation of Hurricane Hugo in 1989 we restored power to an average of 38,000 customers per day, and after a 1996 ice storm, 66,000 customers per day. Each time we have learned valuable lessons about communicating with our customers as we work to safely restore their comfort and security.

One of the realities of the energy business is that many factors are beyond our control – like the weather and the economy. Our job is to effectively manage the factors we can control, and to make the best possible decisions to successfully guide our company through all kinds of conditions and market cycles. Driving us will be our operational focus, our commitment to customers and our belief in the future of competitive energy markets.

“ Trading and  
marketing scandals  
have eroded trust  
in the energy  
industry. What are  
you doing to regain  
that trust? ”



**RICHARD J. OSBORNE**  
EXECUTIVE VICE PRESIDENT  
CHIEF RISK OFFICER

## THE CRISIS IN CONFIDENCE IN ENERGY TRADING IS INDUSTRY-WIDE, AND REQUIRES INDUSTRY LEADERSHIP.

Every company involved in energy trading and marketing is responsible for restoring market confidence and vitality.

As a founding member of the Committee of Chief Risk Officers (CCRO), Duke Energy is working with more than 30 other companies to develop best practices for energy trading and marketing. These standards will make wholesale energy businesses easier for investors, customers and regulators to understand and compare, through better reporting of the risks and financial aspects of their operations.

The CCRO has identified best practices in a number of areas – corporate governance, financial controls, risk management and measurement, including credit risk, and disclosures about trading and marketing operations. Duke Energy is already in compliance with many of the CCRO's recommendations; we're in the process of implementing others, and reviewing our own practices against these new industry standards.

### We've hardwired new control measures into our risk management and trading practices.

We consolidated our risk management oversight functions to ensure a uniform approach and the application of industry best practices across all of our businesses, as we measure and monitor our exposure to both credit risk and energy commodity price risk.

Increasingly sophisticated risk limits allow us to better monitor our market exposures. We're enhancing both energy and credit risk management by clarifying accountabilities, improving measurement criteria, and updating our documentation and reporting practices. We're implementing new risk management information systems to summarize and capture data faster and more accurately, improving our ability to track results. And most importantly, while our corporate and business unit risk management professionals understand the technical and analytical aspects of risk management, they also know that effective risk management means more than monitoring a series of measures and limits – it means understanding the overall risk of an operation or position in a very practical sense.

We've also created a trade operations compliance group. This group studies trading rules and regulations, creates policies and procedures, clarifies standards, provides training and monitors our operations for compliance.

### If we find problems, we move quickly to fix them.

"Round-trip" trades – simultaneous or prearranged transactions that lack a legitimate business purpose, and are conducted for the purpose of increasing volume or revenues – are against company policy. In response to a Securities and Exchange Commission investigation of energy companies' trading practices, we conducted a thorough review of 750,000 transactions going back to 1999, and uncovered 89 such transactions. The round-trip trades totaled less than one-third of one percent of our trading revenues for that period, and had no material impact on earnings.

We publicly reported the transactions, took appropriate disciplinary action and strengthened our controls. Governmental entities continue to review the practices of Duke Energy and other companies that trade energy commodities. This scrutiny should encourage a less risky, better controlled wholesale energy market.

Trading and marketing are the lifeblood of a healthy, competitive energy industry. But they are still somewhat new to the industry. We're working from the inside out, calibrating our controls and policies, and from the outside in, collaborating with industry partners and regulatory bodies, to restore order and trust to this emerging business.

“ What are you doing  
to strengthen the  
company's financial  
position? ”

“ How are you  
improving your  
financial  
transparency? ”



**ROBERT P. BRACE**  
EXECUTIVE VICE PRESIDENT  
CHIEF FINANCIAL OFFICER

**WE ARE TAKING A DISCIPLINED APPROACH, FOCUSING ON OPERATIONAL EFFICIENCY, CASH GENERATION AND CAPITAL MANAGEMENT.**

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We are focused on cash generation, capital management, limiting discretionary spending and reducing our debt. We issued \$1 billion in equity in 2002 to enhance our balance sheet, and we've sold non-strategic businesses and assets. To improve cash flow, we've cut costs, significantly reduced capital spending and focused on the productivity and efficiency of our operations.

In 2003, we expect cash flow from operations, including divestitures, to more than adequately fund capital expenditures of approximately \$3 billion and the approximately \$1 billion needed for the yearly dividend of \$1.10 per share. As of year-end 2002, we had nearly \$2.9 billion in unused bank credit available, in addition to more than \$850 million cash on hand.

In spite of our lowered credit ratings, we have been able to access the capital markets on favorable terms. In 2002, we borrowed at an average interest rate of 6.1 percent, which compares favorably to an average rate of approximately 7 percent for our total debt portfolio.

**WE ARE PROVIDING MORE INFORMATION SOONER, AND MAKING IT EASIER TO UNDERSTAND.**

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Summary cash flow and balance sheet information, for example, is now included with our quarterly earnings releases and simultaneously posted to our Web site. And, we strongly support industry initiatives, legislative reforms and accounting guidelines that bring more clarity to financial reporting.

Duke Energy is providing more detailed information to investors regarding its energy marketing and risk management activities – in fact, we were among the first to provide additional disclosures consistent with those recently recommended by the energy industry's Committee of Chief Risk Officers.

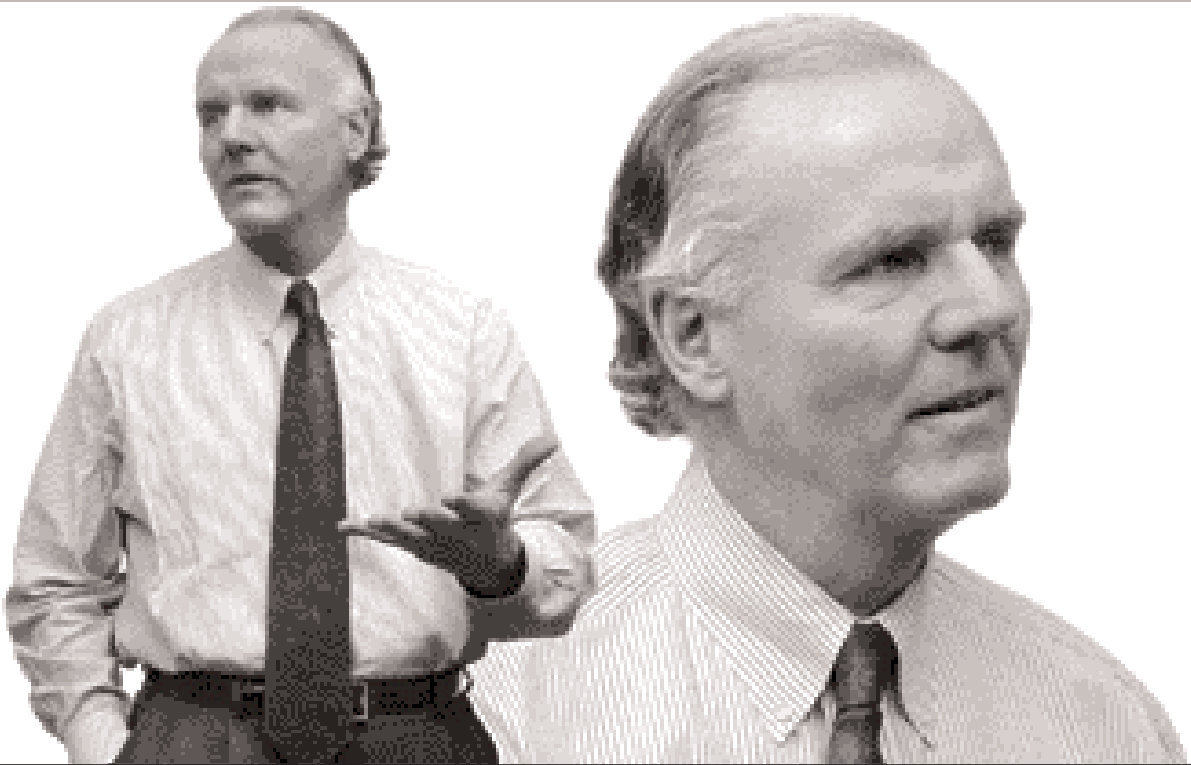
A Financial Accounting Standards Board task force recently ruled that companies could not recognize as earnings unrealized gains or losses on the future value of certain energy contracts prior to settling those contracts. That is, energy companies may no longer use "mark-to-market" accounting to recognize earnings on their income statements, except in certain limited cases. We applaud this ruling, as it removes the uncertainty inherent in applying mark-to-market accounting across the board, provides greater transparency and brings less volatility to earnings.

Another new accounting rule requires that energy companies report trading revenues on their income statements on a net basis instead of a gross basis. This change affects reported revenues, but it has no impact on the company's profitability or cash flows. Measures such as operating income, earnings per share and return on equity have not been affected by this new ruling.

Financial reporting, in my view, should present a fair and complete picture of a company's financial health. Our financial reports undergo rigorous management review and analysis, business by business, before they are published. During 2002, we improved this process to incorporate new requirements as a result of the Sarbanes-Oxley Act. New steps include more detailed discussions and documentation, and a corporate Disclosure Committee reviews our financial reports before they are filed with the Securities and Exchange Commission. These activities are designed to ensure that our published financial reports continue to accurately, clearly and thoroughly reflect the financial condition of Duke Energy and its businesses.

“ Your longstanding reputation has been challenged. What are you doing about it? ”

“ New regulations and legislation are changing corporate governance practices. How does your Board of Directors measure up? ”



**RICHARD W. BLACKBURN**  
EXECUTIVE VICE PRESIDENT  
GENERAL COUNSEL  
CHIEF ADMINISTRATIVE OFFICER

## OUR REPUTATION IS BUILT ON ACTIONS, NOT JUST WORDS.

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The Duke Energy name has historically stood for integrity and fair play. That perception has been challenged. We've worked hard and long to build our good name, and we intend to preserve it. Ethical conduct is, and always has been, a defining aspect of our company, and a key competitive advantage.

Earning the public trust is no easy task. It starts by making sure our house is in order.

We've taken a critical look at what we do, and how we do it. Our values – integrity, stewardship, inclusion, initiative, teamwork and accountability – are more than ideals posted on a wall. They're the way we do business, from the board room to the break room. We weave them into our corporate policies and procedures, into our very culture. They underlie contracts written for mutual benefit, as well as legal obligation. And they are key factors in the way we recruit, select and train employees, and guide their performance.

Over the past year, we have reinforced with employees Duke Energy's business values, emphasizing their relevance to every task and decision. We've also updated our Code of Business Ethics, to clarify how the values apply in specific situations. We're not perfect – but we take prompt and decisive action if we find that our Code of Business Ethics has been violated.

## OUR BOARD OF DIRECTORS PROVIDES ETHICAL AND ACCOUNTABLE LEADERSHIP.

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Mistrust of corporate governance due to real and perceived abuses has given rise to new legislation and regulation – in the energy industry and throughout the business world. Our corporate governance remains strong and accountable, and in compliance with recent reforms.

Even before the Sarbanes-Oxley Act was signed into law in 2002, Duke Energy's policies and practices guarded against conflicts of interest, supported independent and involved oversight of management by the Board of Directors, and provided other safeguards now required by the legislation. For example, since 1993, Duke Energy has provided employees with a telephone hotline to anonymously report suspected violations of law or of the company's Code of Business Ethics. And a recent policy change prohibits senior officers from using the company's external auditor for any personal services.

We have further strengthened our policies and practices to reflect the requirements of the Sarbanes-Oxley Act. Duke Energy prohibits loans to executive officers, for instance, and this year the board's Audit Committee will begin pre-approving all services provided by Duke Energy's auditor.

New governance rules proposed by the New York Stock Exchange (NYSE), and under review by the Securities and Exchange Commission, require that companies have written governance principles. We've had written principles since 1998. In addition, we've had practices in place that reflect other NYSE proposed, but not yet required, standards. For example, the members of our Board of Directors' Audit, Compensation and Corporate Governance Committees are independent. And, the Corporate Governance Committee reviews directors' and executive officers' service on other boards for possible conflicts of interest, and to ensure they can adequately focus on their responsibilities to Duke Energy's shareholders.

Duke Energy welcomes these constructive reforms. But what they say is true: "You can't legislate morality." There's no substitute for a commitment to the ethical core of this company. Our board, our management, our employees and our auditors are accountable for fulfilling both the spirit and the letter of the law. That's the kind of responsible performance that will get our industry back on track.