



Management's Discussion and Analysis

This Discussion and Analysis is a review of the results of operations, and outlook for SaskEnergy Incorporated (SaskEnergy or the Corporation) and its subsidiaries for the three month period ended March 31, 2006. This discussion should be read in conjunction with the consolidated interim financial statements and accompanying notes. For additional information relative to its operations and financial position, refer to the Corporation's Annual Report for the year ended December 31, 2005.

Corporate Profile

SaskEnergy has the legislated franchise for the distribution and transmission of natural gas within Saskatchewan. The distribution system provides natural gas service to over 329,000 residential, farm, commercial and industrial customers over a 66,000 kilometre pipeline distribution system. The transmission system provides transportation and storage service to the distribution system, producers, marketers and large volume end-use customers within Saskatchewan.

SaskEnergy has seven wholly-owned subsidiaries:

- TransGas Limited – owns natural gas transportation and storage facilities;
- Many Islands Pipe Lines (Canada) Limited – transports natural gas to and from other jurisdictions and is regulated by the National Energy Board;
- Bayhurst Gas Limited – owns, produces and sells natural gas from storage-related assets and holds natural gas royalty interests;
- SaskEnergy International Incorporated – holds international equity investments;
- Swan Valley Gas Corporation – owns a natural gas distribution utility in the Swan Valley area of Western Manitoba;
- Saskatchewan First Call Corporation – operates an underground infrastructure facility database through which subscribing companies are alerted of the need to perform line locates for landowners or contractors planning to excavate in Saskatchewan;
- SaskEnergy Nova Scotia Holdings Ltd. – holds SaskEnergy's interest in a natural gas distribution utility in Nova Scotia.

Financial and Operating Highlights

	Three months Ended March 31	
	2006	2005
Financial Highlights		
Consolidated Net Earnings (millions)	\$37	\$35
Total Assets (millions)	\$1,332	\$1,246
Long-term Debt (millions)	\$653	\$675
Operating Highlights		
Distribution		
Volumes Distributed – Petajoules	42	49
Winter Weather – Compared to the thirty year average	9% Warmer	3% Colder
Average Cost per Gigajoule of Natural Gas to March 31	\$8.76*	\$6.88
Transmission		
Volumes Transported – Petajoules	114.6	102.0
Peak Day Natural Gas Flows (Winter Season) – Petajoules	1.53	1.38
– Date of Peak Flow	February 16	January 15

*Before the effect of the Saskatchewan Energy Share

Financial Results

Consolidated Net Earnings

The two major components of consolidated net earnings are earnings from operations and the gain or loss on commodity sales. For the first three months of 2006 consolidated net earnings were \$36.9 million consisting of earnings from operations of \$36.3 million plus a \$0.6 million gain on commodity sales.

In comparison, consolidated net earnings were \$34.8 million for the first quarter of 2005 as the earnings from operations of \$31.6 million were lower than 2006 and the gain on commodity sales of \$3.2 million was higher in 2005.

A. Revenue

1. Delivery Revenue

Delivery revenue in the first quarter of 2006 was \$57.2 million, which was \$4.9 million lower than the same period in 2005. The majority of SaskEnergy's distribution customers consume natural gas for heating purposes and, as a result, the volume of natural gas distributed is sensitive to variations in weather, particularly through the November-to-March prime heating load season. The weather from January 1 to March 31, 2006 was 11.2% warmer than the same period in 2005, resulting in reduced delivery volumes and revenue.

2. Transportation and Storage Revenue

Transportation and storage revenue for the first three months of 2006 was \$22.9 million, which was an increase of \$1.4 million over the same period in 2005. The increase is mainly due to incremental revenue generated by two new storage caverns.

3. Net Sales from Gas Marketing

In order to maximize the utilization of its assets during off-peak periods, SaskEnergy purchases and sells natural gas in the open market and earns a margin. SaskEnergy also supplies natural gas to large end-use customers in Saskatchewan through a competitive bidding process.

The Corporation also owns underground natural gas storage facilities that are no longer used in commercial storage operations. The natural gas from these facilities is being removed and sold in the open market.

In the first quarter of 2006, net revenue from the foregoing activities was \$9.1 million compared with \$1.9 million for the same period in 2005, primarily due to higher volumes sold in 2006.

B. Expenses

Total expenses to March 31, 2006 were \$64.8 million, which were \$0.6 million lower than the first three months of 2005.

Operating and maintenance expenses for the first quarter of 2006 were \$29.4 million which were \$0.1 million higher compared to 2005.

Interest expense was lower by \$0.9 million for the first three months of 2006 compared to 2005 due to a reduction in both over-all debt levels and average interest rates.

Amortization of property, plant and equipment of \$12.8 million was \$0.5 million higher in 2006 due to a higher asset base in 2006.

Payments to municipalities to March 31, 2006 were consistent with the same period in 2005.

C. Gain on Commodity Sales

Similar to practices in other Canadian regulated jurisdictions, SaskEnergy's commodity rates are designed to ensure that, in the long term, the Corporation neither profits from, nor incurs a loss on, the sale of natural gas to its commodity customers. Commodity rates are set on a periodic basis, whereas natural gas purchase prices are subject to monthly price volatility. As a result SaskEnergy may experience gains or losses on commodity sales within any reporting period.

In response to record-high natural gas prices in the fall of 2005, the Government of Saskatchewan introduced the Saskatchewan Energy Share. The intent of the Saskatchewan Energy Share was to effectively cap the price consumers would pay at \$7.95 per gigajoule (GJ) from November 1, 2005 to March 31, 2006.

During the first quarter of 2005 the commodity rate charged to consumers was \$6.97 per GJ compared to the cost of gas sold of \$6.88 per GJ. The resulting gain on commodity sales in the first quarter of 2005 was \$ 3.2 million.

During the first quarter of 2006 the commodity rate charged to consumers was \$7.95 per GJ which was lower than the cost of gas sold of \$8.76 per GJ. Therefore, in the first quarter of 2006, SaskEnergy was eligible to receive \$20.5 million from Saskatchewan Energy Share which resulted in a gain on commodity sales of \$0.6 million.

Effective April 1, 2006 the commodity rate charged to customers was decreased from \$7.95 per GJ to \$6.80 per GJ.

Outlook

The earnings of SaskEnergy are influenced by changes in a number of factors. The following are the factors that can cause the greatest variability in earnings:

Description of the risk	Factor	Sensitivity	Impact on annual net earnings	
			Decrease	Increase
Natural gas prices fluctuate in the market and can affect earnings if there is a change in the market price per gigajoule with no accompanying change to SaskEnergy's approved commodity rates.	Natural gas prices	\$0.10 change per gigajoule	Higher gas prices \$(5.4)	Lower gas prices \$5.4
Natural gas prices fluctuate in the market affecting earnings by changing the sale price of storage gas volumes sold by Bayhurst Gas Limited.	Natural gas prices	\$0.10 change per gigajoule	Lower gas prices \$(0.6)	Higher gas prices \$0.6
Foreign exchange can affect earnings as a change in value of Canadian currency relative to United States currency impacts natural gas prices in Canada. This in turn may affect commodity purchase costs incurred by SaskEnergy.	Foreign exchange impact on natural gas prices	\$0.01 change to foreign exchange rates	Weaker CDN \$ \$(4.7)	Stronger CDN \$ \$4.7
Winter weather fluctuations can affect earnings. Revenue forecasts are based on the assumption of normal winter weather defined as the average weather experienced over the last thirty years.	Winter weather	One per cent change in winter weather	Warmer than normal \$(0.7)	Colder than normal \$0.7
TransGas receipt contracted volumes are affected by the capacity contracted by shippers for the transportation of their natural gas.	TransGas receipt contracted volumes	One per cent change to contracted levels	Decreased contracting \$(0.6)	Increased contracting \$0.6
Short-term interest rates affect the cost of short-term borrowing.	Short-term interest rates	0.25 per cent change in short-term interest rates	Increased rates \$(0.2)	Decreased rates \$0.2

(\$7.0) (\$3.5) \$0.0 \$3.5 \$7.0
(\$ millions)

The above sensitivities are intended to be illustrative of the relationship between the variables and financial performance and are not intended to reflect management's view as to the likelihood of this variability.

SaskEnergy Incorporated
Consolidated Statement of Financial Position
(thousands of dollars)

	<u>As at</u> <u>March 31, 2006</u> <i>(unaudited)</i>	<u>As at</u> <u>December 31, 2005</u> <i>(audited)</i>
Assets		
Current assets		
Cash	\$ 6,795	\$ 1,572
Accounts receivable	233,439	215,614
Natural gas in storage held for resale	84,570	139,255
Inventories of supplies	7,137	7,346
	<u>331,941</u>	<u>363,787</u>
Property, plant and equipment (net)	940,569	946,947
Investments and other assets	30,867	32,225
Natural gas in storage held for resale and operations	28,201	28,030
	<u>\$ 1,331,578</u>	<u>\$ 1,370,989</u>
Liabilities and Province's Equity		
Current liabilities		
Short-term debt	\$ 65,300	\$ 80,500
Accounts payable	182,846	237,591
Dividend payable	12,700	5,200
Current portion of long-term debt	64,342	71,637
	<u>325,188</u>	<u>394,928</u>
Long-term debt	588,643	582,279
	<u>913,831</u>	<u>977,207</u>
Province of Saskatchewan's equity		
Equity advances	71,531	71,531
Retained earnings	348,081	323,878
Foreign currency translation adjustment	(1,865)	(1,627)
	<u>417,747</u>	<u>393,782</u>
	<u>\$ 1,331,578</u>	<u>\$ 1,370,989</u>

(See accompanying notes)



Director



Director

SaskEnergy Incorporated
Consolidated Statement of Earnings and Retained Earnings
(thousands of dollars)

	Three months ended March 31	
	<u>2006</u>	<u>2005</u>
	<i>(unaudited)</i>	<i>(unaudited)</i>
Revenue		
Delivery	\$ 57,239	\$ 62,139
Transportation and storage	22,868	21,468
Revenue collected for municipalities	9,812	10,261
Net sales from gas marketing	9,092	1,918
Other	2,032	1,222
	<u>101,043</u>	<u>97,008</u>
Expenses		
Operating and maintenance	29,414	29,282
Interest	11,407	12,264
Amortization of property, plant and equipment	12,805	12,330
Payments to municipalities	9,812	10,261
Saskatchewan taxes and royalties	1,314	1,257
	<u>64,752</u>	<u>65,394</u>
Earnings from operations before the following	<u>36,291</u>	<u>31,614</u>
Commodity revenue	176,651	167,621
Cost of gas sold	(196,569)	(164,465)
Saskatchewan Energy Share	20,530	-
Gain on commodity sales	612	3,156
Net earnings	<u>36,903</u>	<u>34,770</u>
Retained earnings, beginning of period:	323,878	276,431
Dividend	<u>(12,700)</u>	<u>(14,300)</u>
Retained earnings, end of period	<u>\$ 348,081</u>	<u>\$ 296,901</u>

(See accompanying notes)

SaskEnergy Incorporated
Consolidated Statement of Cash Flows
(thousands of dollars)

	Three months ended March 31	
	<u>2006</u>	<u>2005</u>
	<i>(unaudited)</i>	<i>(unaudited)</i>
Operating Activities		
Net earnings	\$ 36,903	\$ 34,770
Add (deduct) items not requiring an outlay of cash		
Amortization of property, plant and equipment	12,805	12,330
Other non-cash items	689	(539)
	<u>50,397</u>	<u>46,561</u>
Net change in non-cash working capital related to operations	<u>(17,676)</u>	<u>29,375</u>
Cash provided by operating activities	<u>32,721</u>	<u>75,936</u>
Investing Activities		
Additions to property, plant and equipment	(9,439)	(8,080)
Customer capital contributions received	3,012	374
Increase (decrease) in natural gas in storage (non-current)	(171)	58
	<u>(6,598)</u>	<u>(7,648)</u>
Financing Activities		
Decrease in short-term debt	(15,200)	(39,900)
Dividend paid	(5,200)	(26,500)
Sinking fund instalments	(500)	(250)
	<u>(20,900)</u>	<u>(66,650)</u>
Increase in cash during period	5,223	1,638
Cash position, beginning of period	<u>1,572</u>	<u>3,637</u>
Cash position, end of period	<u>\$ 6,795</u>	<u>\$ 5,275</u>

Cash position consists of cash and cash equivalents less bank indebtedness.

(See accompanying notes)

SaskEnergy Incorporated
Note to the Consolidated Financial Statements
March 31, 2006
Unaudited

1. Accounting Policies

SaskEnergy Incorporated (SaskEnergy or the Corporation) prepares its consolidated interim financial statements in accordance with Canadian generally accepted accounting principles except that the disclosures do not conform in all respects to the requirements for annual financial statements. The consolidated interim financial statements follow the same accounting policies and methods of computation as the consolidated financial statements for the year ended December 31, 2005.

These consolidated interim financial statements, which are unaudited, should be read in conjunction with the consolidated financial statements for the year ended December 31, 2005 and have been prepared from the records of the Corporation. The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets, liabilities, revenue and expenses. Actual amounts could differ from these estimates.

The consolidated interim financial statements should not be taken as indicative of the performance to be expected for the full year due to the seasonal nature of the natural gas utility business in Saskatchewan.

2. Saskatchewan Energy Share

In November 2005, the Government of Saskatchewan approved an appropriation of \$123,940 thousand to establish the Saskatchewan Energy Share. The appropriation relates to the period November 1, 2005 to March 31, 2006 as it was designed to assist natural gas consumers in dealing with high natural gas prices during the winter of 2005/2006.

The Saskatchewan Energy Share included a specific appropriation of \$92,040 thousand to be used by SaskEnergy to cap the cost of natural gas sold to customers at \$7.95 per gigajoule during the period November 1, 2005 to March 31, 2006. For each month during this period, SaskEnergy calculated its actual cost per gigajoule of natural gas and compared this amount to the cap of \$7.95 per gigajoule. Based on estimates of sales volumes, SaskEnergy's actual cost of gas for January, February, and March 2006 was above the cap of \$7.95 per gigajoule and accordingly, SaskEnergy received \$20,530 thousand from the Saskatchewan Energy Share.

Certain natural gas consumers in Lloydminster, Saskatchewan receive their natural gas service from Direct Energy Regulated Services (a supplier based in Alberta). Under the Saskatchewan Energy Share, \$1,000 thousand was allocated to provide eligible Lloydminster customers with a one time credit of \$200. This credit was provided to these customers in 2006. During the month of March 2006, SaskEnergy reimbursed Direct Energy Regulated Services for these credits and in turn recovered this amount from the Saskatchewan Energy Share. The cost of this initiative was \$549 thousand.