

In an evolving climate, those that are agile and adaptable survive. Those that combine these traits with a solid strategic core thrive. We are such a company.



- After approximately a decade of preparing for retail electric competition, in mid-2002, the Arizona Corporation Commission changed its generation divestiture policy, resulting in APS remaining a vertically integrated utility. We quickly adapted to this reversal of direction and demonstrated our ability to remain agile in the face of changing regulatory and marketplace climates.
- We continue to meet the changing needs of our customers. Since 1999, our peak load has grown 18 percent, while we have continued to improve our reliability measurements.
- Streamlined processes and a more productive workforce allow us to do more with less. In 1998, we served approximately 775,000 retail electric customers with about 5,900 employees\*. In 2002, we served more than 900,000 customers with approximately 6,100 employees.
- Process and workforce improvements also enable us to keep generation production costs low. In 2002, our nuclear and coal production costs averaged 1.68 cents per kilowatt-hour, well below expected national averages.
- We continue to have a diverse generation mix. By 2004, our estimated generation mix will consist of roughly 43 percent coal, 31 percent nuclear and 26 percent natural gas. This diversity will allow us to continue effectively managing risk in the face of changing wholesale markets and fuel prices.
- We continue to offer customers greater flexibility, and reduce our operating costs through our utility Web site – APS.com. In recognition of these efforts, APS.com was named Best Energy Site for 2002 by the Web Marketing Association, a national organization made up of Internet marketing, advertising, public relations and design professionals.

*\*Employee counts reflect workforce serving retail electric business*

# Our region continues to grow rapidly. Growth is our future and we will manage it to benefit our customers, our shareholders, our employees and our state.

- APS experienced 3.1 percent customer growth (nearly 30,000 new customers) in 2002 – about three times the national average. Our customer base is projected to continue to grow about 3.5 percent annually in the next three years.
- Much of this growth occurs in the heart of our service territory – the greater Phoenix area. The Phoenix metro area issued nearly 41,000 building permits in 2002 – ranking second among the 10 largest metropolitan areas in the United States in building permits per 1,000 residents.
- As our customer base grows, we also are expanding our power resources. By bringing on line two new gas-fired units at the Redhawk Power Plant and a new unit at the Saguaro Power Plant, we added more than 1,000 megawatts of new generating capacity in 2002. In addition, a 530-megawatt unit at the West Phoenix Power Plant is expected to be completed in summer 2003, and the 570-megawatt Silverhawk Plant in summer 2004.
- As an internationally recognized leader in the research and development of solar technology, we are dedicated to finding renewable energy solutions for future generations. In 2002, APS began construction of the Prescott (Ariz.) Airport Solar Power Plant, which, when completed, should be the largest photovoltaic solar plant in the world. Completion of the solar plant is expected in the next five years, when the facility's capacity will reach 5 megawatts.
- We expanded our transmission and distribution system in 2002, adding nearly 800 miles of wires. On average, a new substation was completed every seven-and-a-half weeks. We also began construction on a 500-kilovolt transmission line that, when completed in mid-2003, will bring needed transmission capacity to support the continued growth of the greater Phoenix area.



The seeds of desert wildflowers lie dormant in the soil for all but a few weeks each spring. Then, if autumn and winter rains have fallen at the right times and in the right amounts, Arizona's desert explodes in a riot of growth and color. Rushing to take advantage of the short period when moisture and temperatures are optimal, desert wildflowers germinate, grow to maturity and bloom in a matter of days. The speed of their growth, the varied colors and the abundance of flowers are startling.

## AVERAGE YEARLY PRECIPITATION

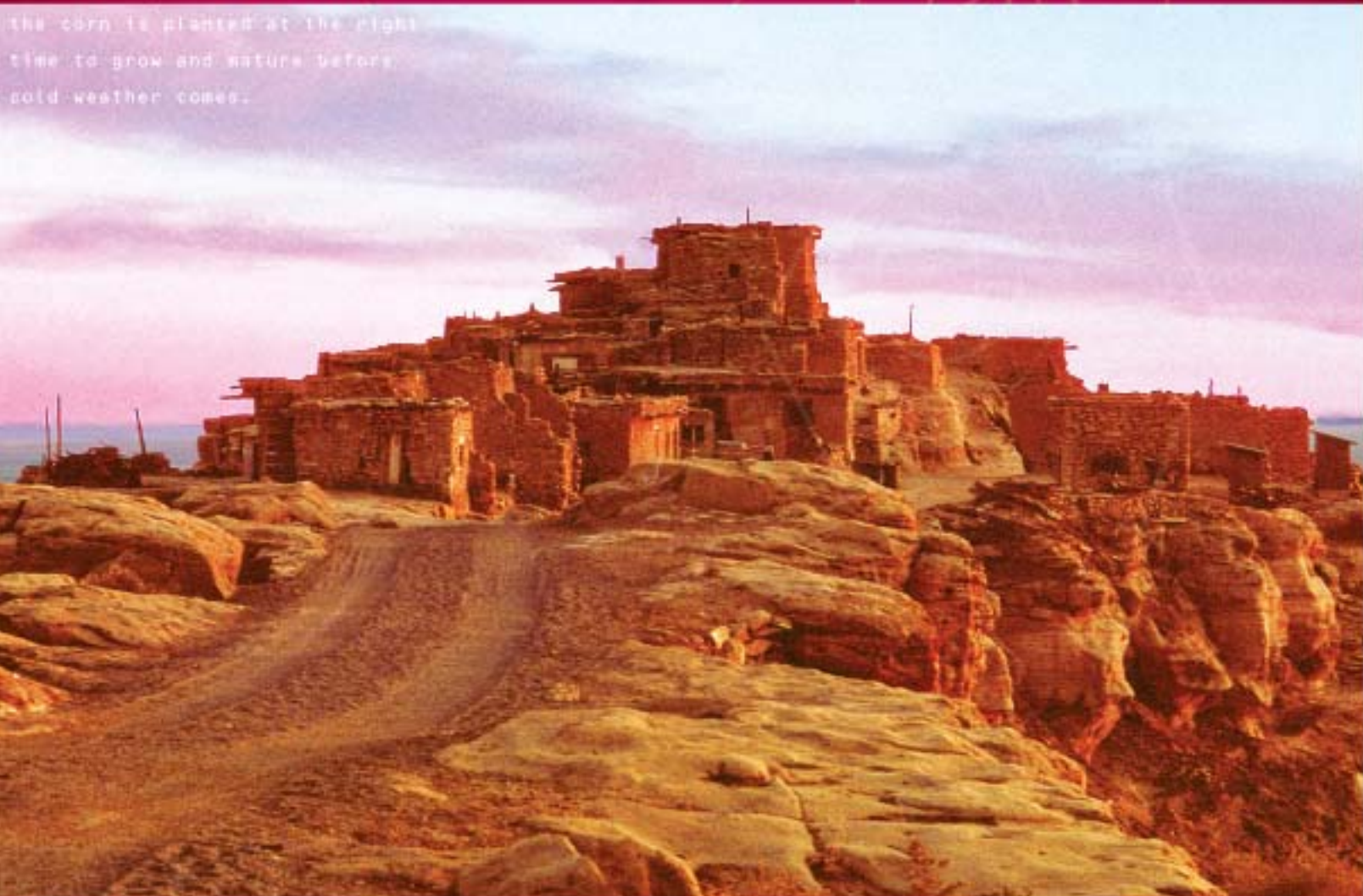
(Rain, Melted Snow, and Ocean Vapors)

Inches	Centimeters
24 to 32	61 to 81
16 to 24	41 to 61
8 to 16	20 to 41





The Hopi, who live on the high, dry mesas of northeastern Arizona, have for centuries observed a strict religion that permeates every aspect of their lives. They have prayers and specific rituals that accompany everything from planting corn to childbirth, to observing the solstices and equinoxes. Many of these rituals are linked to survival, such as assuring the corn is planted at the right time to grow and mature before cold weather comes.



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# A strong plan is important. Execution of that plan is vital. Our people continue to perform and raise the standards by which we measure success.

- Our fossil power plants operated at high levels throughout 2002. The five coal-fired Four Corners units achieved a combined capacity factor of 83 percent, placing the site in the top 20 percent in the nation. Our Cholla coal plant and the combined gas and oil plants at Ocotillo, Saguaro, West Phoenix, Yucca and Douglas had availabilities of more than 90 percent.
- In 2002, the Palo Verde Nuclear Generating Station produced a national record 30.8 billion kilowatt-hours of electricity, breaking its own record of 30.4 billion kilowatt-hours set in 1999 and repeated in 2000.
- Palo Verde also operated at a best-ever 94.4 percent capacity factor and marked its eleventh consecutive year as the number one power producer of any kind in the United States. This focus on efficient plant production continues to be exceeded only by our intense focus on plant safety.
- We continue to believe areas such as safety, financial integrity, business practices, community involvement and environmental stewardship are key ingredients in creating shareholder value. We emphasize continuous improvement in our safety record and again reduced our number of preventable recordable injuries.
- We grew our common dividend 6.3 percent in 2002. Our dividend growth over the past five years averaged 7.2 percent per year and ranked number one among U.S. electric utilities.
- Pinnacle West again earned the top rating (AAA) for environmental, economic and social performance from Innovest, an international investment advisory firm. The firm ranked us number two out of the 28 electric utilities included in the S&P 500. We also were presented the Better Business Bureau of Central and Northern Arizona's Business Ethics Award.

# Our roots run deep in Arizona and the West. We've been here for 116 years. We know the landscape. We know the people. We know the opportunities.

- APS has reduced customer electricity prices 14.5 percent since 1993. This number will reach 16 percent in mid-2003 and represents the largest cumulative price decrease among investor-owned utilities nationwide in that time period. These reductions have saved our customers more than a billion dollars.
- In the 2002 electric utility customer satisfaction studies conducted by J.D. Power and Associates, APS residential and midsize business customers rated us higher than any other investor-owned utility in the western region.
- In a year of low wholesale energy prices and a market in which most industry power marketing functions lost millions, our Power Marketing group effectively managed wholesale risk and contributed more than \$100 million of pretax gross margin to our company.
- In its fourth year of operation, APS Energy Services, our competitive retail energy services company, continued to carve a profitable niche for itself by providing integrated solutions from commodity energy to energy efficiency-related products and services. In 2002, APS Energy Services began \$40 million worth of energy efficiency work for Arizona's three major universities, continued adding commercial and industrial commodity customers in the West and contributed more than \$28 million to pretax earnings.
- SunCor, our real estate development company and one of Arizona's premier home-builders, had a strong financial year as well, contributing \$19 million to earnings. SunCor is also expected to make cash distributions to Pinnacle West of \$80 million to \$100 million annually from 2003 to 2005 from matured asset sales. In 2002, the company opened its newest development, the 1,850-acre StoneRidge golf community in Prescott Valley, Ariz. Nearly 140 homes and 20 custom home sites had been sold at StoneRidge by the end of 2002.

