



SPEED BUMPS & POTHOLES ON THE ROAD TO ELECTRIC COMPETITION

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Constellation NewEnergy: The Advertisement

- The nation's largest "all-markets" provider of competitive retail electric power.
- A leading provider in Northern Illinois.
- Active developer of tailored products for end-use customers.
- Affiliate of Baltimore Gas & Electric and Constellation Power Source.
- Constellation owns/operates two power plants in Illinois (near Effingham & University Park).

Electricity is a Network Industry Headed toward Competition

- All network industries have now moved toward competitive structures to replace end-to-end franchised monopoly models.
- Transport fully competitive: rail, air, truck.
- Telecommunications largely competitive.
- Energy (gas & electric) is hybrid.
- The process that began in the U.S. in the late 1970s has stayed largely on track to introduce competition where possible in network industries traditionally operated as “natural monopolies.”

The Underlying Rationale for the Movement to Competition

- Regulated network industries are largely mature and have been extended widely in society.
- The traditional network regulated monopoly model extends control to many otherwise competitive elements and activities.
- Regulated monopoly tended to support distortions & inefficiencies that competition will purge.
- Technology has been altering the industry functionality and relationships in the market.
- Capital can be attracted at reasonable cost and risk in the context of competition.

If All You Knew Was the Past 2 Years You Would Not Be Crazy to Doubt the Rationale

- California, Enron, El Paso, United Airlines, US Air, Qwest, WorldCom etc.
- Are networks over-extended and are they even contracting?
- Employment has been hard-hit?
- Investors & lenders are battered.
- Has the rush to newer technologies too rapidly made the older ones obsolete?
- Are we really getting efficiencies and accurate pricing and by what measure?

But What's the **REALLY BIG** Picture?

- The movement toward a competitive industry structure is not slowing down appreciably.
 - FERC SMD NOPR confirming new structures
 - Transmission assets are being sold
 - Generation continues to devolve to EWGs
- Consumers show an increasing appetite for choice among energy providers and specialized products.
- Capital markets are discovering the differing risk profiles of industry functions and elements.
- Little constituency for re-verticalization.

Competition in Electricity is Producing the Promise

- In spite of industry “turmoil” customers outside the West have had attractive pricing
- Substantial new generation came on line the past three years and the forward price curve suggests low prices for some time ahead.
- Competitive retail products are better meeting customers’ consumption patterns.
- The nuclear industry is largely revitalized.
- Utilities continue to look for greater efficiencies.

What Can We Expect from Policy Makers the Next 2 Years?

- We are unlikely to see Federal legislation but the FERC SMD NOPR is likely to largely take effect.
- The states that have adopted competitive policies will stay largely on course.
- California will gradually “re-accommodate” competition.
- In “non-competitive” states, business customers will increasingly be given versions of choice.

What Can We Expect from the Capital Markets?

- There will be a natural reluctance to invest in power plants in regions with surpluses.
- Wires companies that have shed supply obligations will be seen as stable entities.
- Private investors will continue to acquire transmission assets and generation.
- Accounting standards will need to address the problems of valuing energy contracts.
- Wholesale energy trading will have more oversight and will be more assets backed and new capitalization norms will develop.

What Can We Expect from the Electric Industry?

- Utilities will continue to disaggregate and more generation will devolve to competition
- Low asset values and differences in stock value will lead to more consolidation.
- Efficiency and competition will likely keep wholesale prices low.
- Retail marketers will develop more products and more businesses will opt for choice.