Portfolio Management: The Post-Restructuring World

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The Big Picture

- Retail Competition isn't working very well
  - Most all customers are on default service
- Investors are shunning power plant investments
- Wholesale markets have been
  - Too volatile
  - Riddled with market power problems
  - Have not demonstrated ability to develop new power when and where needed – Resource Adequacy

State Policy Response

- Stop pretending retail service is competitive
- Assign duty to acquire a longer term, diverse resource portfolio to distribution company (or other entity)
- Put Energy Efficiency back in the picture *as a resource*
- Reconnect SBC $ to economic analysis
- Try to improve use of emerging wholesale markets through competitive bidding

What Actions are States Taking?

- California – portfolio management assigned to stand alone distribution companies
- Arizona – portfolios with contracts of diverse length, efficiency and renewables come first, then disco shops for supply side
- Arkansas – restoration of what looks like IRP with emphasis on competitive purchases in wholesale markets

Regulation Deals with Risks

- Familiar old risks
  - Fuel cost increase
  - Capital cost increase
  - Economic conditions/ demand for product
  - System reliability
  - Environmental costs
  - Abnormal weather events
  - Adequate capacity

New Risks

- New Risks in Competitive Markets
  - Market price volatility
  - Market manipulation
  - Resource Adequacy
- Default Service Risk
  - Having all load subject to same/ or nearly same contract period
- System Security/Terrorism

Diversification

- Don’t want all the eggs in one basket
- Diversify
  - By length of commitment
  - By amount of load subject to any single arrangement
  - By resource type
  - By use of Financial as well as Physical assets

Risk Management Options

- Long Term Portfolio – 15 year outlook
- Multiple, overlapping arrangements
- Diversified Resources (Physical)
  - Contracts for output of plants
  - Ownership of power sources
  - Energy Efficiency (Reduce volatility of demand)
  - Renewable resources (No fuel cost, low enviro risk)
- Financial Hedges
  - Need to turn into physical asset at some point
  - Unlike other commodities, we can’t tolerate shortages

Sample Portfolio

% Forecasted Need	Commitment Length	Resource Time Frames
10%	Spot Market	
10%	2 year	
10%	4 year	efficiency
20%	6 year	
20%	8 year	
10%	10 year	
10%	15 year	renewables
5%	20 year	
5%	30 year	

What Does This mean for Market Transformation Activities?

- MT remains important part of the picture
  - Several states have chosen to emphasize MT, even where they did not adopt retail competition
- But there will be increased interest in Efficiency *as a resource*
- Increased emphasis on:
  - Verified savings
  - Shorter time frames