Portfolio Management:
The Post-Restructuring World

Cheryl Harrington
April 15, 2003
ACEEE Market Transformation Conf.
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

<table>
<thead>
<tr>
<th>% Forecasted Need</th>
<th>Commitment Length</th>
<th>Resource Time Frames</th>
</tr>
</thead>
<tbody>
<tr>
<td>10%</td>
<td>Spot Market</td>
<td></td>
</tr>
<tr>
<td>10%</td>
<td>2 year</td>
<td></td>
</tr>
<tr>
<td>10%</td>
<td>4 year</td>
<td>efficiency</td>
</tr>
<tr>
<td>20%</td>
<td>6 year</td>
<td></td>
</tr>
<tr>
<td>20%</td>
<td>8 year</td>
<td></td>
</tr>
<tr>
<td>10%</td>
<td>10 year</td>
<td></td>
</tr>
<tr>
<td>10%</td>
<td>15 year</td>
<td>renewables</td>
</tr>
<tr>
<td>5%</td>
<td>20 year</td>
<td></td>
</tr>
<tr>
<td>5%</td>
<td>30 year</td>
<td></td>
</tr>
</tbody>
</table>
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