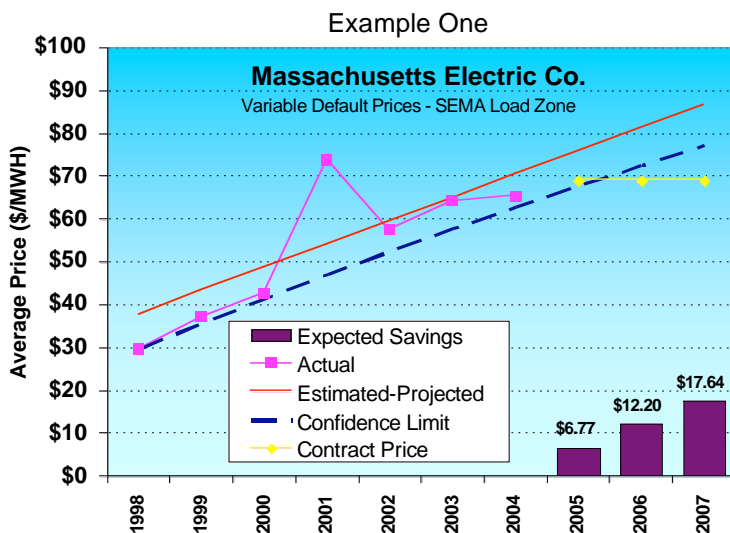




Making Sense of Moving Markets

As the impending extinction of Standard Offer rates in Massachusetts illustrates, the era of fixed electric tariff rates is quickly passing. Electric rates in many EDCs today are now set several times a year, monthly in others and, in the case of larger accounts in New Jersey and Maryland, hourly. Buyers seeking the solace of a fixed price are now faced with a dilemma: What is a good price? How will it compare with utility rates over a year or more?

Determining those answers requires new analytical tools to support buying decisions. The chart below labeled Example One presents one such tool for projecting utility rates in Massachusetts Electric



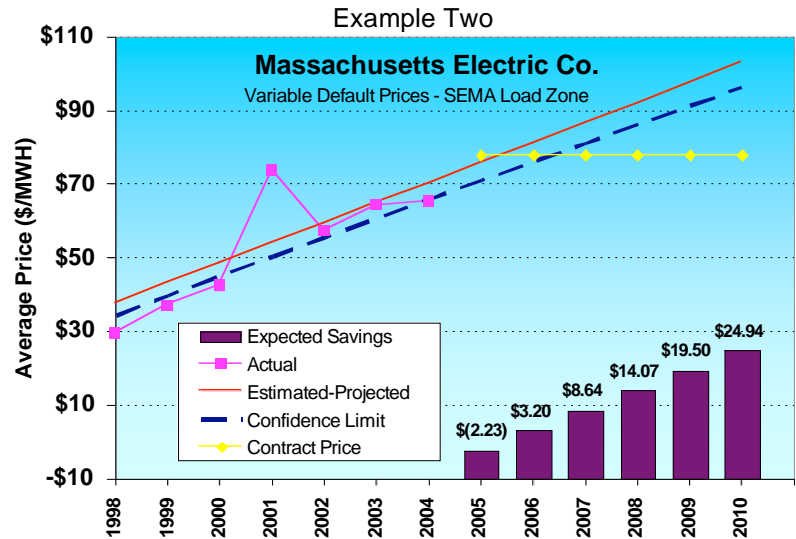
Company (MECo). In it, we used the actual monthly default prices from 1998 through 2004 (broken magenta line) and regression analysis to generate a trend line illustrating expected future values (orange line). We then plotted a dotted-blue line showing values for a targeted confidence level of 70% that the contract price would beat the actual price in each year of a three-year contract. The yellow line represents a fixed-price bid of \$69 remaining steady over the three-year term. The purple bars in the lower corner show the expected \$/MWH value of the savings in each year of the proposed contract term. The trend clearly suggests

default prices will continue to increase over time. The confidence that expected savings will not be overcome by short-term reversals in the trend is much greater with longer term (2-5 year) than with shorter-term contracts. In addition, the longer-term contracts provide greater budget certainty and reduced procurement effort and cost.

This particular model allows the user to specify a desired confidence level and account-specific historical usage data, offering the opportunity to frame expectations for a given procurement opportunity. The table marked Example One correlates to the above graph and illustrates a fictional electric purchase for a company with two big-box retail locations in MECo's SEMA load zone. The desired term of the contract is 24 months. The projected price for the contract term using the regression tool is \$80.21/MWH. A target confidence level of 70% was entered, yielding a target strike price of \$71.91/MWH. The buyer received a low bid of \$69.00, a price that presented an actual confidence level of 76% that savings will be realized over the contract term. In this case, expected savings between the trend price and contract price would represent just over \$60,000.

EXAMPLE ONE	
TERM	24-Month
TOTAL USAGE (kWh)	5,407,200
PROJECTED PRICE	\$ 80.21
TARGET CONFIDENCE	70%
PRICE @ TARGET CONFIDENCE	\$ 71.91
ACTUAL BID (\$/mwh)	\$ 69.00
ACTUAL CONFIDENCE	76%
EXPECTED SAVINGS (\$/mwh)	\$11.21
EXPECTED SAVINGS (%)	14%
EXPECTED SAVINGS (\$)	\$ 60,629

A second example assumes that a longer-term option is desired and illustrates the point that even a purchase entered into at a price higher than that indicated as initially reasonable by the trend line could actually be quite advantageous over the long haul. In it we assume a 72-month contract term, during which time the average electric cost is projected to rise to \$90.71 (or \$80.74 with a confidence level of 70%). The expected utility price at the beginning of the term is \$75.77. Let's suppose that the buyer receives and accepts an offer of \$78.00, or \$2.33 higher than the initial expected price. This price actually yields a 75% confidence level that savings will be achieved over the 72-month period. If the trend were to hold true, these savings would represent more than \$206,000.



EXAMPLE TWO	
TERM	72-Month
TOTAL USAGE (kWh)	16,221,600
PROJECTED PRICE	\$ 90.71
TARGET CONFIDENCE	70%
PRICE @ TARGET CONFIDENCE	\$ 80.74
ACTUAL BID (\$/mwh)	\$ 78.00
ACTUAL CONFIDENCE	75%
EXPECTED SAVINGS (\$/mwh)	\$12.71
EXPECTED SAVINGS (%)	14%
EXPECTED SAVINGS (\$)	\$ 206,201

It is important to remember that the slope of the trend line, or the rate of price increase or decrease, will change over time as new prices are set and more data informs the model. The model will also not account for changes in prices brought about by new or changing regulations or economic dislocations. It does, however, provide a reasonable basis for decision-making in an environment where default prices are being increasingly set more closely to, and more often by, wholesale energy markets. In other words, the one we find ourselves in today.