UEM PULSE, THE NEWSLETTER DEVELOPED FOR THE UNDERSTANDING ENERGY MARKETS SUBSCRIER BASE. DESIGNED TO PROVIDE SUBSCRIBERS WITH UPDATES ON UEM RESEARCH AND EVENTS IN THE RETAIL MARKETPLACE.

INSIDE THIS ISSUE

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"Keeping Your Finger On the Heartbeat of Energy Markets"

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The Sizzling Summer of 2000: How Did Residential Customers Respond?

The summer of 2000 was a difficult one for both competitive electricity suppliers and residential customers — as least according to news accounts. Skyrocketing wholesale electricity prices in California were passed on directly to customers — at least in San Diego. Higher than expected wholesale prices on the East Coast reportedly led some competitive suppliers to return customers to the LDC. These combined events led some commentators to proclaim the failure of competitive retail electricity markets. But how have customers responded? Do residential customers, particularly those that have selected competitive electricity providers, agree with these pronouncements? Are competitive market customers, and particularly switchers, concluding that competition was a bad idea?

THE SHORT ANSWER IS NO, at least according to a new telephone survey of just over 400 residential customers in three competitive states (California, New Jersey, and Pennsylvania). Just over 300 "non-switchers" (customers that have stayed with their LDC throughout their customer experience) and 117 switchers (customers who have chosen to purchase electricity from a competitive electricity supplier, at least at some point) were surveyed in September/October of this year.

How Do Customers View Competitive Markets?

A full two-thirds (65%) of switchers in these three states believe that deregulation is "a good idea and working well," or "a good idea that could be improved." Non-switchers are less positive (50%) but still more likely to have these positive views than to think that deregulation "has caused a lot of problems," or "is a bad idea" (23%). Among switchers, only 20% have these negative assessments of the way deregulation is working.

These assessments are consistent with answers to a question about what should be changed in the way electricity deregulation works in their state. Among switchers, 61% thought that deregulation "should continue as it is now," or that only "minor problems" should be corrected. Among non-switchers, a smaller group (52%), though still a majority had these positive views. Just 13% of non-switchers and 8% of switchers thought that deregulation "should be stopped."

It was interesting to note that switchers were more likely than non-switchers to believe that competition has both "increased prices" and "decreased prices." Among switchers, for example, 35% believe that competition has increased prices, while 30% believe that competition has reduced prices. Among non-switchers, 25% believe prices have increased, while 14% believe they have decreased Non-switchers, as you would expect, tend more to believe that competition has had no effect on electricity prices, or to say they do not know what impact has occurred. What is interesting here is that both groups are probably right. In all likelihood, competition has not changed the price paid for electricity

(Continued on page 3)

Additional UEM Products Planned

As part of our ongoing effort to provide UEM subscribers with more value, we are developing several new research areas and product/report to be made available to subscribers by the end of the year (or shortly thereafter). These research efforts have been designed to offer you with more insight, and more information, about retail energy markets than you have ever had before.

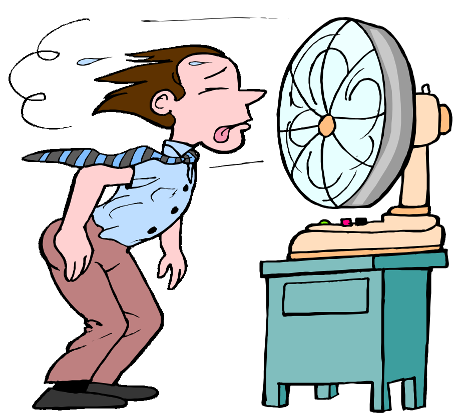
Value-Added Service Compilation

As regulated utilities explore the options that will be available to them under the variety of market opening rules that may exist, many feel that they need to maintain an understanding of the non-commodity products and services being offered by other traditional vertically integrated utilities, distribution companies, and competitive retail electricity providers. At this point, a relatively wide variety of electricity service features, non-commodity, but still energy-related, products and services, and non-energy-related products and services are being offered to residential customers, mass market business customers, and larger business customers. Understanding which features, products and services are being offered where, to whom, and by whom, provides the basis for both understanding the competitive landscape and understanding the lessons that have been learned so far about what can be efficiently provided to customers, and which of these items provide customers with additional value.

This work will identify and organize a database of currently offered value-added services by company and by customer segment. We also expect to maintain this list of actively sold products and services over time.

Retail Market Overview

The year 2000 has been an eventful one for competitive retail energy markets in the US. Competitive electricity markets, never very robust since their outset (or at least since the wrap-up of pilot programs in New Hampshire and Pennsylvania) saw dramatic reductions in activity among both retail providers and customers. In light of the importance of the movement to, and the changes in, competitive retail markets in 2000, EPRI has conducted several pieces of work evaluating different elements of those markets. Under the UEM target, for example, EPRI has conducted research on customer response to competitive opportunities, changes in customer attitudes across competitive and non-competitive states, the growth in value added products and services in competitive markets, and other related issues.



Similarly, Primen has conducted its own research on competitive market activity, and has analyzed prior EPRI research (Share Wars) for insight into the retail opportunities that may exist in competitive markets but which are not currently being mined by competitive suppliers.

While much research on specific issues relevant to the overall assessment of competitive retail markets has been conducted, by both EPRI and Primen, there is no single resource that attempts to integrate, synthesize, and draw implications from those multiple lines of inquiry. Work in this new project area is designed to close that gap. We believe that existing research on this subject can be mined to tell a powerful story about what has happened so far in competitive retail markets, why it has happened, and what it all means for the future of electricity competition.

Key to the execution of this work will be a retail issues summit, currently scheduled for the week of December 11, 2000. The goal of this two-day meeting is to bring together Primen staff, EPRI staff, key disco representatives, key ESP representatives, regulatory observers, and others to review what current research and observations really tell us about the future of retail markets. A key output of this activity will be a set of scenarios that describe possible retail market outcomes.

Residential Competitive Response 2000

The summer of 2000 has been an interesting one for residential electricity customers in deregulated markets. This time period has seen the expansion of competition to several new markets, while at the same time,

(Continued on page 4)

(Continued from page 1) Sizzling Summer of 2000

among non-switchers (at least in most geographies, and depending on how one interprets negotiated across-the-board rate cuts), while switchers may well have seen either higher or lower prices (or both).

Are Customers Happy With Their Choices?

Among switchers, 54% say that they are "happy" with their decision, while the next largest group (23%) say that they have seen "no big differences" as a result of switching. Just 6% of switchers say they regret their choice to switch. This trend is reinforced by the finding that the the "biggest drawback" mentioned most commonly by switchers (60%) that has resulted from switching is "nothing" (16% mention either higher prices, or discounts not as low as expected). As you might expect, 63% of switchers say they switched for price, with the next most common reason given (15%) was "environmental" issues.

How Satisfied Are Switchers With Their New Providers?

The survey asked both switchers and non-switchers to rate their satisfaction with several different specific elements of service on a 10-point scale on which "1" represented "Very dissatisfied" and "10" represented "Very Satisfied." The story that emerges from reviewing top-two-box scores (ratings of either "9" or "10" on the 10-point scale) across these items, is quite interesting, if nothing else because it differs so much by state (focusing on just two states for now).

In Pennsylvania, the difference is clear; non-switchers rate their traditional utility supplier higher on a variety of specific performance attributes, including price, customer service, environmental friendliness, and related characteristics by from 10-25 percentage points as compared with the way that switchers rate their suppliers. On price, for example, 39% of non-switchers give their provider a top-two-box score, while among switchers, just 29% give the same rating. For customer service, the gap is 60% to 44%, while for commitment to the environment it is 43% to 23%, for courtesy, helpfulness, and knowledgeability of employees it is 54% vs. 44%, and for customer service quality overall, it is 55% vs. 40%.

Scores for satisfaction reflect these differences, though not so dramatically. Pennsylvania non-switchers give more top-two-box scores on overall satisfaction than do switchers, but only by a difference of 6 percentage points (54% vs. 48%).

In California, the situation is more complicated. Non-switchers rate their traditional utility more positively than switchers rate their competitive energy supplier on customer service-related attributes (by around 10 percentage points). Switchers, however, rate their company more positively than do non-switchers on environmental issues (by a large 30 point margin), and are equal on ratings for price and commitment to the local economy. It is also worth noting that Californians of both categories rate their suppliers much less positively on price than do Pennsylvanians; just 10% of non-switchers and 14% of switchers in California, for example, give top two box ratings on price, vs. 39% and 29% for the same groups in Pennsylvania.

As is true in Pennsylvania, non-switchers in California also rate their current provider higher on overall satisfaction, compared to switchers, but by a smaller margin than we might expect (29% vs. 24%).

The Bottom Line

In both states, non-switchers tend to have a more positive view of their current electricity provider than switchers have of their current electricity provider. This difference is more pronounced in Pennsylvania, since in California, on two attributes providers are rated equally, and on one attribute (environment) switchers rate their provider more positively.. Switchers, in other words, are worse off — by their own admission — compared to non-switchers in both states, but less worse off in California.

Now for the other side of the story. Pennsylvanians in both groups rate their current electricity provider much more positively than do Californians in the same group. Non-switchers in Pennsylvania, for example, are much more positive about their supplier across the board than are non-switchers in California (by 20-30 points). The same is true of switchers. Pennsylvania switchers are much more satisfied with their new providers than are California switchers (by 15-20 points), except on environmental friendliness, where Californians are more positive.

The end result: Pennsylvanians are more satisfied than Californians with their electricity service, while non-switchers are more satisfied than switchers (generally). But across the board, in terms of overall satisfaction, while non-switchers are more satisfied than switchers, the difference is not as large as we might expect given the differences in scores on the individual item measures. Why is this? Why do switchers "forgive" their providers on their overall satisfaction scores ("Yes," they say, "you're bad on all the specific items of performance, but overall you're not so bad")?

Look for the full report on this work later this year for more answers.

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(Continued from page 2) ***Additional UEM Products***

a variety of competitive providers have decided to abandon some markets and turn their hard-won customers back to the distribution company.

In San Diego, retail prices soared as wholesale price volatility was passed on directly to customers. Questions abound as a result of these outcomes. Are customers, as well as regulators, now ready to give up on competition? Are providers looking to abandon competitive markets completely? If not, what do they need in order to remain as active players in retail markets? If the indicators of success in competitive markets are an active field of competitive suppliers and significant numbers of customers choosing to do business with those suppliers, what will be necessary in order to yield that outcome?

The goal of this work is to explore the reaction of both competitive providers and residential customers, to things that happened during the summer of 2000, and to explore the implications of these outcomes for the future of competitive energy markets. Some of the findings of this work are described elsewhere in this issue of *Pulse*, but note that a more complete description of these results, and the response database, will be provided to you before the end of the year. Look for this report to provide the best available information about how customers are really reacting to retail market events, and to provide insight about how these responses might vary across states.

ETHNOGRAPHIC RESEARCH: What are You Looking At?

You may not realize it, but somebody may be watching your every move. Leading corporations in many industries including high-tech, food, and consumer products have learned they can respond to, and anticipate, rapidly changing and competitive markets by incorporating well-focused, timely ethnographic research into their product development process.

Ethnography is a social science research method which relies heavily on up-close, experience-near participation (**not** just observation) by ethnographic researchers, often working in multidisciplinary teams. It usually includes a blend of historical, observational, and interview methods.

Ethnographic methods are a means of obtaining local points of view, a means of identifying significant categories of human experience up close and personal. Ethnography enhances and widens top-down views and enriches the inquiry process while generating new analytic insights by engaging in iterative, team exploration of often subtle arenas of human difference and similarity.

This type of research has been utilized by numerous companies including Rubbermaid, Motorola, and Johnson Controls, just to name a few. These companies observe or videotape consumers using products. The goal is to capture consumer behaviors and patterns in context, rather than gather information through surveys or questionnaires. Survey results often are incomplete since there is a difference between what people say they do and what they actually do or need and what they actually do or need.

Johnson Controls, for example, uses video ethnography to help auto makers differentiate their vehicles with new interior designs and features. Researchers strategically place four small cameras strategically in a family's car and ask the family to go about its daily routine. Observing families in this way has uncovered information that would not be revealed otherwise. Seeing women drivers look through their purses in the passenger seat, for example, led to a more user-friendly center console as well as organizers built into a fold -down passenger seat. Watching consumers load items into cars and mini vans led to trunk organizing systems.

Primen recently applied ethnographic research methods in the field in a project for EPRI's Strategic Science & Technology Group. Research teams including an engineer and a social scientist (typically an anthropologist) visited sites consisting of large office buildings, manufacturing facilities, and biotech facilities. The teams' mission was to identify unarticulated customer needs that would lead to the identification of a set of novel product/service concepts. The teams developed a fundamentally new way to conceptualize building processes and needs and identified what may well be breakthrough opportunities for energy service providers to offer value to customers. Call Patricia Garber at Primen if you would like to explore how to apply these methods at your company.