

# Leveraging the tactics of energy risk management available in Illinois' competitive market

*How competitive energy suppliers are delivering a range of options designed to help small and large businesses better manage risk in energy purchasing and shield exposure to volatile market prices*

**M**anufacturers have traditionally viewed energy costs as a significant and unpredictable line item on their budget. Today's volatile energy markets and fuel prices make it nearly impossible to budget accurately, leaving businesses dangerously vulnerable as they face erratic price swings. In Illinois and states across the country, manufacturers and businesses have an alternative. Competitive energy suppliers are offering and continuing to develop new products and programs to meet a wide variety of consumers needs, namely stabilizing energy costs and providing budget certainty.

As we know, energy costs are among the most volatile in the commodity market. Anything from severe weather to political uprisings half way across the world to an oil spill can directly affect your daily prices. When faced with this type of uncertainty, it's necessary for energy consumers to take measures to reduce their risk of exposure and establish a predictable energy delivery and pricing strategy. Suppliers such as Constellation NewEnergy are working with manufacturers in Illinois and businesses throughout North America to do just that by offering a range of energy solutions with varying degrees of risk tolerance.

Let's take a look at some of the basic energy purchasing strategies available today. In order to better understand the available options, one can generally distinguish two components that make up a customer's electricity bill – the energy itself (i.e. electricity) and all other related charges, such as charges for

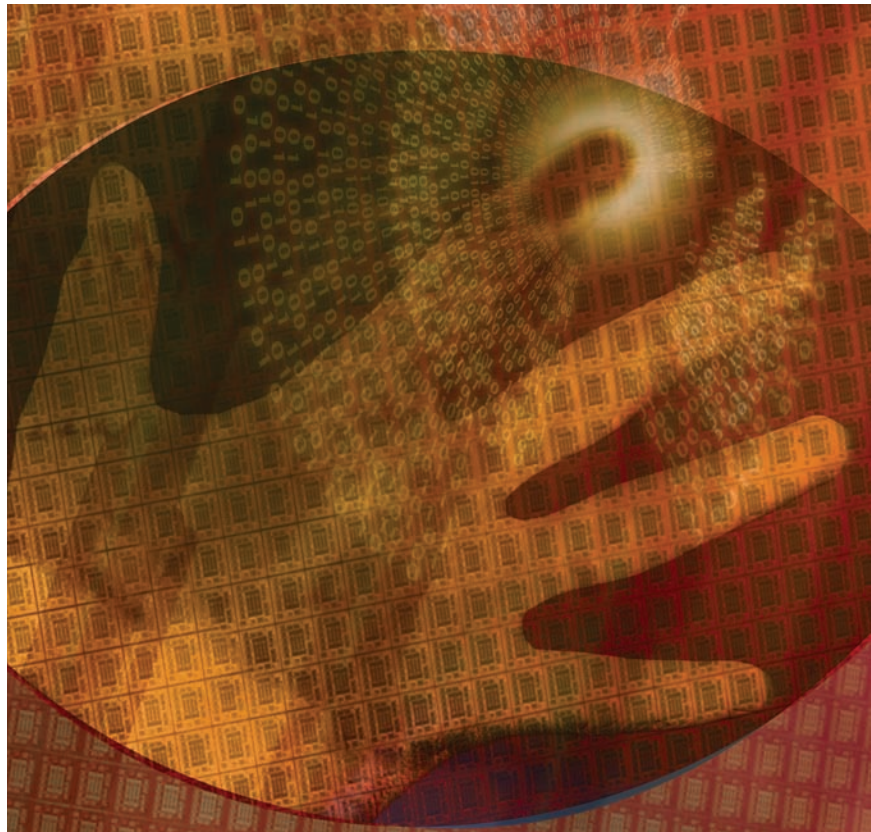
delivering the energy to the customer, the cost for making energy available, and taxes. Energy charges usually constitute the largest piece of a customer's invoice and are subject to much greater volatility.

## **Solutions that minimize risk and maximize stability**

We'll begin with an energy solution designed particularly for the customer that requires the security of predictable monthly electricity expenses. A fixed price energy agreement can guarantee 100 percent sta-

bility in energy costs, which in turn alleviates any concerns of variable energy charges, fluctuating utility rates, or market price spikes for the length of the contract. Fixed pricing agreements can be customized to meet both short and long-term requirements, can be combined with locking in the price for some or all non-energy components, and most importantly, allow customers to more accurately budget and forecast future electricity spending.

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**Scott Lewis** is Sales Director for Constellation NewEnergy, a leading competitive energy supplier for commercial and industrial customers that serves the Illinois manufacturing industry. He can be reached at [scott.lewis@constellation.com](mailto:scott.lewis@constellation.com).

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One step down from the total cost stability delivered by a fixed pricing agreement is a flexible index solution. A customer can purchase a percentage of their daily energy consumption (or for example their on-peak hourly usage) at a fixed price, and float the remaining usage on the daily index market. Businesses that choose this approach maintain a hedge against volatile price swings and also open the door to potential savings. By accepting some risk to purchase on the spot market for a short period during the day, businesses gain the advantage of potentially securing lower market prices during such hours. If the daily market price is below the contracted fixed price, customers can spend less than they would have with a 100 percent fixed price agreement.

Manufacturers with greater control over their energy consumption needs are well positioned to benefit from a flexible index pricing option.

For businesses that closely watch energy consumption, shifting load to more favorable hours under this model can significantly lower energy spending.

For manufacturers willing to take even slightly more risk, a block plus index solution is available, which enables consumers to lock in a more specific portion of their electricity demands or tailor their supply to meet a particular need.

Businesses that actively monitor and manage electricity consumption patterns are well suited to explore this option. Similar to flexible index solutions, block plus index pricing goes beyond distinguishing solely between on and off peak demand.

Block plus index solutions allow a customer to further narrow down their primary consumption parameters and select a block of time for which they choose to lock in a fixed energy price. Blocks can be purchased at any time for standard market periods or for a period of months. The duration of time and amount of electricity within a block is determined by the customers'

individual needs. Any electricity consumption that falls outside the block index pricing is billed at the variable index price. If the customer uses less than the block purchase, the excess energy will be sold back into the spot market and the customer will be credited with such amount.

Each electricity pricing option gives customers the ability to further specify components of their agreement, including the choice to bundle all non-energy charges such as ancillaries, line losses, distribution, and transmission into a fixed price charge. This action can further reduce exposure to risk and help avoid unexpected charges on the monthly bills. Constellation NewEnergy customers in Illinois and North America also gain free access to the NewEnergy Online (NEO) web-based energy management and budget tracking tool. NEO is providing customers of all sizes with detailed electricity market information, customized energy tracking and usage history, comparison features that can help identify efficient or

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inefficient equipment, and an overall better understanding of the factors that drive market prices, as well as impact budgeting activities and the bottom line.

### Advanced energy hedging strategies

Lastly, for large-scale energy consumers looking to set more aggressive budget targets beyond the capabilities of the above mentioned risk management purchasing strategies, Constellation NewEnergy offers a sophisticated energy hedging program entitled i2i (information to implementation). Modeled after financial risk management strategies, the i2i program analyzes a customer's risk profile and designs an optimal energy procurement strategy to meet each customer's budgetary requirements. The company's i2i patent-pending analytic model assesses budget goals, risk tolerance, and the global market factors impacting each customer to aid in the development of a roadmap, which guides the energy purchases

made on behalf of the customer.

i2i customers are free to take as little or as much risk as they'd like. The tradeoff remains the same: those willing to accept a wider margin of risk also position themselves for greater rewards, as well as the potential to meet or exceed more aggressive budget targets. Constellation NewEnergy provides the expertise necessary to help customers navigate the treacherous landscape of energy markets to make calculated and informed energy purchases. The i2i program is structured around a long-term approach (3-5 years), which is necessary to leverage market volatility by taking advantage of market lows to shield against market highs. This strategy has proven effective in bringing energy costs back under control and helping customers achieve long-term budgetary goals.

Here in Illinois, CB Richard Ellis (CBRE) enrolled in the i2i program in 2005 and has since seen measurable results. Budget expectations have been surpassed and in comparison-based studies, CBRE has outperformed its peers by significantly reducing its energy costs. With the

i2i program, CBRE is able to combine the energy procurement and expenses for 16 of its facilities to improve efficiencies and manage costs at a corporate level rather than at a facility level. Most notably, CBRE was able to achieve these impressive results and manage through the volatile price spikes during Hurricanes Katrina and Rita to achieve long-term price stability and meet its budget targets.

Illinois manufacturers and energy consumers have the advantage of operating in a competitive energy market where suppliers such as Constellation NewEnergy have rolled out a range of energy purchasing and risk management programs. CNE's programs are designed to help customers stabilize energy costs and bring more certainty to the budgeting process. Regardless of the size, scope, or energy needs of a manufacturer, implementing some form of hedging strategy or risk management approach towards the purchase of electricity will undoubtedly make a positive impact on the bottom line. ■



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