E-business – the real threats and opportunities

Most utilities now recognise that e-business[1] will impact their activities. Almost every company has a web presence, and some have even won awards for the quality of their web site. Many are developing closer links with their suppliers through virtual market places, and with their customers through interactive web sites and on-line customer service facilities. Some have developed extensive intranets for sharing information within the firm, and others have even established electronic links with their strategic partners in order to work more closely and effectively.

Utilities, analysts, investors and consultants have conducted numerous surveys, examining the quality, reliability and functionality of the web sites of the major players, and assessing the extent to which the various utilities are involved in B2B ventures or joint procurement initiatives. These surveys can reveal useful information on the preparedness (or otherwise) of the incumbent utilities. For example, a recent report by PA Consulting[2] on the adoption of e-business by utilities in the UK, Australia and Scandinavia indicates that that utilities may be focusing too much attention on B2C activities (interactive web sites etc.) and not enough on the impact of B2B activities (shared procurement portals, energy broking etc.) which we consider will have a much larger commercial impact: Indeed, if it becomes the norm that large organisations procure all their requirements (including energy) through price based virtual hubs, this will have a major impact on the way that utilities sell energy.

However, we consider that many of these surveys are limited in that they focus upon what the utilities are doing/not doing. We believe that e-business can and will have a major impact on what companies do and how they are structured. In response to growing regulatory and competitive pressures, and driven by the ability of e-business to reduce costs, streamline operations, and allow multiple groups to share information, we expect companies to reassess the various activities that they undertake, and to outsource, insource, sell, and grow business activities to reflect their particular strengths and aspirations.

There may well be some interim consolidation (to gain economies of scale in particular activities), but then many of the super-utilities will find it advantageous (and possibly more politically acceptable) to split into specialist businesses, each of which will be a major player in their own market. We have identified five main business functions: customer service; marketplace (including B2B); risk management; outsourced services; and infrastructure ownership. These are described below:

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[1] E-business is defined here as ‘the use of Web technologies to streamline business processes, share information, increase revenues and decrease costs’.

[2] ‘Potential e-nergy? Releasing the full potential of e-business in the utilities’. This is available from PA Consulting or on the Web at http://www.pa-consulting.com/utilities/energy_report.html

- **Customer service** organisations will offer a bundled product to customers for a range of utility services. Some will sell their own energy supply, while others will act as independent intermediaries that seek out the best deal for the customer. Examples include essential.com (independent intermediary) and Centrica (both independent (for telecoms) and own supplier (gas, electricity, financial services)).

- **Risk management** organisations exist because of basis risk, price volatility, etc. These companies manage their sales, purchases, storage, and pricing of electricity and gas to offer a wholesale product with reduced price volatility. They sell this product to customer hubs and large commercial/industrial consumers. Examples might include Enron and TXU Europe (in the UK gas market).

- **Marketplace** organisations will add value by bringing together buyers and sellers, through exchanges, auctions, or catalogues. The Internet through its ubiquitous accessibility makes it easy and cheap for participants to join, and this added liquidity increases competition and reduces transaction costs. Altranet.com is one example of a vertical (industry-specific) exchange, whereas Ariba.com is an example of a large 'catalogue' type organisation. We consider that customer pressures will force vertical exchanges to offer a wider range of services, and horizontal catalogues to offer more detailed industry information so buyers can make informed decisions.

- **Outsourced services** companies already exist: well-known examples include 24seven (network asset management), and Vertex (United Utilities' customer service function). Many of these companies that have not yet separated out these functions (such as Centrica), manage their internal service functions as profit centres in an internal market, and these compete for funds and are often benchmarked against external service providers. We expect that some of these may well be split out and sold in response to competitive and regulatory pressures.

- **Infrastructure owners** range from network utilities (gas and pipelines) to generation units (tolling plant) in which all the business functions and market risks have been stripped away. These assets are then bond-like in performance. Offering an annuity is more suited to debt than equity funding. Examples of emerging asset companies include BG, which is leveraging its regulated pipeline assets (Transco), and Drax power station, which was purchased by AES with 80% project financed debt.

These businesses within the utility conglomerate have very different risk/reward profiles, and we therefore consider that the pressure of shareholder expectations will force them to be split out and probably listed separately, certainly refinanced more cheaply, and their market value will reflect more closely their particular risk characteristics.

Many companies appoint a dedicated e-business team (either internal or external) reporting to a senior manager to look at the strategic implications of e-business. Several recent surveys use the size and composition of these teams and whether a Board member has explicit e-business responsibilities as a measure of the importance that a company places upon e-business.

However, we think that this may not be a meaningful measure: we consider that examining e-business opportunities is not and should not be the prerogative of a select few in the IT or strategy team. Rather, it should be the responsibility of all senior managers (perhaps supported by IT people) to assess what implications the Internet holds for them. For example, web page development should be reflect the requirements of corporate PR people (who deal with shareholders), internal communications people (in so far as the internal communications are made available through the web), and customer service people. Similarly, we would expect decisions about joining an on-line procurement group to be made by those people responsible for cost-effective procurement, rather than by a team of IT enthusiasts and technophiles.

Indeed, one can go still further: it could be argued that the Internet and e-commerce are not different (except in terms of scale and pervasiveness) from other forms of communication, and that long term, the web will be just another part of a senior manager's skillset. As one person in the PA survey commented: 'e-business is really everyone's business'.

In summary, we offer the following comments on e-business and its implications for utilities:

1. Analysis of the e-business activities of incumbents can be useful but may focus attention on the wrong things: B2B activities (within and outside the firm) will have far more impact than B2C activities

2. Liberalisation and e-business developments are likely to lead to major changes in the market: restructuring along functional lines is inevitable given the new economics of business operations.

3. E-business should not be the responsibility of a small team isolated from the corporate centre: instead, a clear understanding of the opportunities and threats should drive the decisions of all senior managers.

Utilities, as a homogeneous group with common characteristics, will soon cease to exist. Whether any individual company, restructured and refocused, will survive long term will depend upon its understanding of threats and opportunities of e-business and the actions it takes in response.

NB. PA announced in July 2000 its intention to acquire Hagler Bailly. Completion is expected in late October 2000, and the new enlarged firm will trade as PA Consulting from that date.