CFO Roundtable

More Strategy in the CFO's Responsibilities

Part I

(Part II to appear in January's PUF)

Bob Frenzel, CFO, Xcel Energy
Drew Marsh, CFO, Entergy
Marty Lyons, CFO, Ameren

With the many changes that our industry is dealing with, and the increased complexities and uncertainties around customer and shareholder value, the position of the chief financial officer has significantly changed.

Managing financial performance and reporting to shareholders is only a small part of the modern CFO's job. They need to understand the impact and possibilities of new technology, changing policies and regulations, evolving customer needs, new products and services, changes in operations and security, and much more.

Chief Need-To-Know-It-All is probably the best way to describe the new, broader and enhanced CFO role and position. We asked three CFOs – Bob Frenzel of Xcel Energy, Drew Marsh of Entergy, and Marty Lyons of Ameren – about their company's aspirations, how they engage with their customers, and how they develop new products and services.

We asked what their challenges and successes are, and what their plans for distributed energy resources and grid technologies are. Their perspectives provide a great behind-the-scenes view of the issues that some of the largest investor-owned utilities are focused on.

– Jan Vrins, managing director and leader of Navigant's global energy practice

PUF's Steve Mitnick: Where do you want your company to be in five years?

Bob Frenzel, CFO, Xcel Energy: We focus on three things. The first is continuing to be a leader in a clean energy transition.

Xcel Energy has been the largest provider of wind to our customers for twelve years in a row. We expect that leadership position to continue. We're also really focused on delivering goods and services to our customers in an economical and affordable way.

Finally, the expectations of customers over the last five or ten years have evolved, and the manner with which we interact with our customers is changing. Products and services that we deliver to our customers are changing.

We aspire to be a valued brand and a valued retail partner to our customers.

Drew Marsh, CFO, Entergy: We are focused on maintaining the lowest retail electricity rates in the country while implementing our nearly eleven-billion-dollar capital plan, and reorienting ourselves around our customers' evolving expectations.

All of this needs to be accomplished while continuing to deliver our broader financial plan for our stakeholders.

Marty Lyons, CFO, Ameren: For the past several years, we've been focused on improving customer satisfaction and optimizing our operations, so we can deliver industry-leading total shareholder return.

As I look out five years, we will be focused on the same goals, believing that meeting our customers' needs remains central to our success.

Customer expectations are changing. There are even greater expectations in terms of reliability, affordability, choice and convenience.

When you look out to the grid of the future, utilities are well-positioned to be at the center of value creation for customers through investments in a smarter and more secure grid.

You must be disciplined enough to take on industry transformation without giving up expectations your shareholders already have for you.

– Drew Marsh

PUF's Steve Mitnick: What are the big challenges?

Drew Marsh: As we move away from a more engineering-centric approach to a more customer-centric one, the challenge is acquiring new skills and capabilities to understand the customer better than we have in the past.

There are new technologies that we can leverage – learning how to use those to invest for growth is going to be important.

You must be disciplined enough to take on this industry transformation without giving up the expectations that your shareholders already have for you.

For Entergy, we're focused on hitting those marks from a steady, predictable growth perspective and an earnings and dividends perspective. The basic services that we provide today are still going to be necessary in five-year scenarios.

Jan Vrins, Navigant: Even those basics – engineering and operations of the grid – are changing. How do you integrate renewables? How do you integrate distributed resources?

Drew Marsh: Adapting all those new technologies, thinking about new ways to work, changing our processes to be more efficient and more customer-centered. We hope we can enhance everything that we are doing.

All the things we are doing today create the opportunity for whatever might be tomorrow.

Bob Frenzel: The operation of these businesses is incredibly complex, and is getting more complex. The serious situations in

both Florida and Puerto Rico highlight the value of the grid and the value of electricity.

However, people have an expectation that things are getting easier to be delivered. Logistics and supply chains are getting easier. You pick Amazon or Uber, and the expectation is, "I want it easy and simple. I don't want to know all the engineering that's happening behind the scenes."

Taking what is a very complex and industrially-challenging business, and placing significant new requirements on it, like an advanced grid, distributed energy resources, or integrating renewables, is a significant challenge for the industry.

We've been able to invest as an industry, and a company, while interest rates have been low. While commodity prices have been low, we've been upgrading the infrastructure of our assets, our networks, our grids, and our generation facilities.

I don't know when and how those factors change over time. But the customer has been the beneficiary of an increased amount of investment, when both those things have been relatively low. We've kept total cost to the customer very limited.

In fact, our bills to our customers have been flat to declining over the past four or five years, even as we've invested significantly into our infrastructure and our networks.

We've been able to invest as an industry while interest rates have been low, while commodity prices have been low.

– Bob Frenzel

Jan Vrins: Do you still think that you'll be able to make investments to integrate distributed energy resources?

Bob Frenzel: I think upgrading the distribution network, focusing on the asset that's closest to the customer, is a very valuable investment to make. An advanced grid enables us to interact with our customers in a different way, in a way that they're increasingly more interested in, while providing value.

Helping customers manage their energy future is important.

Without the investment, I don't think we can get there. But the new technology isn't necessarily free. We're trying to invest cost-effectively.

Marty Lyons: I see many of the industry challenges equating to opportunities. For example, customer expectations are increasing, and customers want higher levels of reliability.

If you look at the past five years, we as a company, our customers and our shareholders, have really benefited from a meaningful investment in transmission to make the grid more reliable.

We have invested almost two billion dollars in transmission projects scheduled to be fully in-service in 2018 and 2019.

That investment makes electricity more affordable by relieving congestion, and allows renewables to move from the west to the east – while also providing greater levels of reliability for the system.

As it relates to sustainability, each of us is investing in universal grid-level solar, and in wind assets. Ameren just announced, last month, an approximately one-billion-dollar investment opportunity associated with seven hundred megawatts of new wind to support our customers.

The rising customer expectations are a challenge. We're up to that challenge. And it's going to present great investment opportunities for utilities.

We have a compelling vision of the grid of the future and the pivotal role utilities can really play in optimizing that future.

We'll be working with stakeholders along the way, to make sure that the right investments are made, and the right regulations are put in place. Modern regulatory frameworks to support investment are essential to meet our customer needs and expectations.

Look at our Illinois distribution operations – constructive frameworks are enabling investment in electric and gas smart meters, which will improve service reliability and give customers information to help them take control of their energy usage and costs.

Encouraging innovation within our companies is something we've been focused on at Ameren for the past few years. We encourage co-workers to think about how things can be different, and how we can incorporate new forms of technology to continue to optimize our business.

Jan Vrins: On the basic product – power – do you see different rate structures there tied to reliability? If my power goes out during the day, I really don't care about that, versus other customers where it's critical.

Marty Lyons: I can't tell you exactly what the rates and tariffs look like in the future. We've already been working with stakeholders as it relates to energy efficiency and certain other programs – modifying how the tariffs and regulatory frameworks work.

But clearly, changes will be needed in order to offer different service levels and tailor offerings to customer preferences.

We must paint a compelling vision of the future by communicating the essential role utilities can play regarding distributed renewables, electrification, battery storage, and other technologies.

And we must work with regulators to put the right kinds of rate structures in place that are fair to all customers.

PUF's Steve Mitnick: Are there good strategies out there to meet these challenges, the expectations for greater reliability, for more interactive grid technologies?

Marty Lyons: Our strategy at Ameren is straightforward. If you think about our history over the past five years, we've really pivoted away from a non-regulated into a fully-regulated business.

We're focused on our 2.4 million electric customers and one million natural gas customers. We seek to identify compelling projects – meaning regulated investment opportunities that are great for customers – and optimizing our business.

Affordability to the customer is key. We must continue to optimize our business, and drive costs down where possible, while working with stakeholders to help everyone understand the benefits of investments for the customer.

We also need to continue to pursue getting the right constructive regulatory frameworks in place to make reliability and other grid technology investments wins for customers and investors.

Bob Frenzel: I'd be remiss if I didn't say "Steel for Fuel" as a value-added strategy. We're taking advantage, in the states Xcel Energy serves, of a unique opportunity to invest heavily in wind generation, as well as other forms of renewable generation, including solar.

We can put wind onto our system and displace fuel – whether it's natural gas or coal – in a cost-effective manner for our customers. We are enabling a clean energy transition through "Steel for Fuel." We're finding it to be cost-effective for our customers and beneficial to our other stakeholders as well.

That doesn't last forever. Wind is a non-dispatchable resource. We have to make sure that we're also caring for the reliability of the grid.

That's going to come with a different set of investment opportunities, such as advanced grid initiatives and automatic switching networks.

We're going to explore things like batteries and other forms of storage. We're going to look at the value of solar in distributed energy resources across our network.

The high-voltage transmission network and low-voltage distribution network are increasingly valuable investments as we get closer to our customer. Enabling our customers to manage their own energy future, whether in the form of rooftop solar, distributed assets, electric vehicles is of increasing importance – and we're prepared to deliver.

Xcel Energy, and our industry peers, are infrastructure enablers. Investing in those types of assets, we think, is a very good strategy for the company.

Jan Vrins: Do you see a point in time where renewables and distributed energy resources become baseload? Combined with storage, with demand response?

Bob Frenzel: I think it's a long way out in the future. But the definition of a long way seems to be changing.

We must paint a compelling vision of the future, communicating the essential role utilities can play.
– Marty Lyons

Ten years ago, we didn't have an iPhone. We didn't have Amazon, Uber, Google, or Facebook as they exist today. What's a long way out seems to be changing.

We put out corporate targets of where we want our emissions profile to be. By the end of this decade, Xcel Energy will reduce our carbon output by forty-five percent from 2005 levels.

By the end of the next decade, we'll be down sixty percent. And we aspire to do that faster.

Technologically, when you get into eighty and one hundred-percent renewables, I think the engineering equation starts to kick in. There are a lot of people looking at the engineering side of the grid reliability equation to see what is the theoretical possibility.

Today I don't see a clear path, but that doesn't mean it can't happen. I'm a two-time engineer. I ran nuclear power plants in the Navy.

This is not a simple engineering problem to solve. Very smart people at EPRI, NREL, scientists and engineers who work on energy storage, are all looking at this, and there are a lot of investments being made to solve this issue.

I don't see the solution today. It could be twenty or thirty years out there. That seems like a long time, but based on how quickly technology is changing it could be here sooner than we think. We need to be prepared.

Drew Marsh: We are still required to put integrated resource plans together in our jurisdictions. There's no way for us to, at this point, simply say that we are going to just build combined-cycle gas turbines or something else on into the future.

We have to absolutely consider these new technologies, the cost curves, the changing nature of storage, and of solar. We don't have as much wind down in Louisiana and Arkansas as you guys do in the Midwest. We have to think about the impact of renewables and those cost curves.

It's also pushing back on the grid. Typically, our grid is one-way today. It starts with central station generation and goes through increasingly small wires to get to the end-use customer.

When you talk about distributed energy resources coming in, you must think about what the impact of that will be on a long-term thirty-year resource plan.

We need to make sure that whatever we're doing is creating value for our customers beyond just creating a list of things to offer them.

– Drew Marsh

Jan Vrins: The way you do load forecasting, transmission and distribution planning, is that changing?

Drew Marsh: Absolutely. Our capital plan for the next five years is clear. Once you start to get past five years, it's going to be much more dependent on the evolution of these different technologies.

Bob Frenzel: We as a company, we as an industry, have been working on speed-to-market. Our customers' expectations are changing rapidly and our ability to adapt to those must accelerate.

While the outside world probably doesn't associate regulated utilities with innovation, in all reality, we have been innovative companies for a century.

Drew Marsh: How does a customer actually achieve value? That is one of the things that we need to think about. Companies have evolved to be very successful up until this point.

As the prospect of a different value-expectation for an individual customer continues to change, the adaptation to meet that is going to be very critical for us.

Jan Vrins: If you make investments in new products and services, do you partner with others? Does the utility become the platform that enables new products and services, whether it's electrification of transportation, distributed generation, storage?

Marty Lyons: What we're doing is very much trying to interact with our customers to understand what's important to them. For a long time, because utilities provided a regulated service, a tariff service, I don't think we were as customer-focused, as customer-centric, as we are today.

Number one, we've got to identify what's important to the customer. And then tailor or customize our product and service offerings to the customers' needs.

In doing that, we have to work closely with regulators to make sure that we're aligned in terms of the need for a particular product and service, and how it's going to be priced.

Also, we must be aligned on where we will play as utilities, and where we will partner with others, to deliver for the customer on their expectations.

I think that's something that we and a lot of other utilities are working our way through right now. I think that as an industry we will continue to evolve our business, products and services, and pricing, to meet changing customer expectations.

Besides interacting with the customers, one of the things we've got to do is really keep our finger on the pulse of technology. This means paying close attention to the rate at which technologies are changing, in terms of both the abilities of technology, and the cost of technology.

We very well could be experiencing exponential change as we look ahead. None of us really know the exact pace of change.

What we have to do is identify those technologies that we think are going to be movers for our customers and for our industry, and then keep our finger on the pulse of that change.

It's important that we constantly work with our customers and our regulators to make sure we're painting this compelling vision of the future, where utilities have this great opportunity to be at the center of meaningful value creation for customers.

Drew Marsh: We need to make sure that whatever we're doing is creating value for our customers beyond just creating a list of things to offer them.

In the past, we considered our customers ratepayers because we delivered a necessary product in a prescribed manner that fit a need, and there was no expectation of service beyond that.

Today, we view our customers as clients with individual needs and preferences, and we are focused on understanding these needs and preferences and identifying opportunities to deliver value well beyond basic utility services.

PUF's Steve Mitnick: As the chief financial officers, historically you're the guys who say no. But now we have the media, the public, regulators, policymakers, people within your company, partners, all coming to you. How do you interpret your role? To say, well, that's cool, but we have to perform our basic job.

Drew Marsh: I would say we're the "yes/if" folks. We realize that we're going to have to make investments.

We're going to evolve. We're going to have to change. The trick for us is to continue to do what we do today well and maintain a disciplined view on capital allocation.

We have to deliver on the promises we've already made, while we begin to incorporate these new things. It's tough because we have to make room. It's going to take a lot of work, a lot of discipline, a lot of rolling up your sleeves, a lot of figuring out how we can create space.

Not just in what's the new whiz-bang technology. But what's the new whiz-bang organization? The new process, the new internal things that we can do to create opportunity. To make room for investment in the future. Data or renewables, or whatever the focus is going to be.

How do we create that space? It's a yes/if conversation. If we can do these other things. Then everybody has to get on board to go make that happen.

Bob Frenzel: I think of the CFO role as being a couple things. First and foremost, we're an enabler of the business.

We deliver electricity or gas to a lot of customers, and whether we deliver a different product, or deliver through a different mechanism, from a financial point of view, we need to enable the business to deliver to our customers.

Second, we're the steward for the providers of the capital. Whether it's the debt holders or the equity holders, we've got to make sure that they're represented in the equation.

I am a believer in the notion that good projects can always find capital.

However, sifting through a myriad of options to find a good project is another role of the CFO. That role of the CFO is to make sure that the good projects rise to the top and allow the rest to filter to the bottom.

That's the big role that CFOs serve internally. I think it's an important one – to be the enabler of business strategy.

We like to say yes, but at the end of the day, we also have to be the guardians.

– Marty Lyons

Marty Lyons: Our roles as CFOs are always going to incorporate capital allocation and putting capital to work in the places that generate the highest returns for shareholders. Our role is not going to change as it relates to disciplined cost control.

There must be good alignment within an organization to commit certain financial resources to new products and services or new technologies. When failure happens, the goal is, "Fail fast, learn from it, and move on."

Many times, it means saying yes to things such as allocating a couple billion dollars to large-scale transmission projects and allocating hundreds of millions to smart meters and grid projects. We like to say yes, but at the end of the day, we also have to be the guardians.

When you want to expand in a certain area, it really demands a business case. What's the market opportunity, the customer demand? What are the financial returns expected to be?

At Ameren, we've been very successful over the past five years at improving, year-over-year, our consolidated earned-return. We have worked to close the gap between our allowed returns and our earned returns.

The rate of growth in our rate base, as we look ahead, is about six percent compounded annually through 2021. We are saying yes to a lot of projects. I think the ones that have the best returns for customers and shareholders have the best business cases and are the ones we say yes to. PUF