



WRITING SAMPLE

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Hospitals Need to Pay Attention to Volatile Energy Market

By Gretchen Heber

Recent significant changes in the Texas energy market have thrown a monkey wrench into hospitals' energy-buying strategies.

The closure this year and last of several coal-fired power plants has increased the likelihood of electricity shortages this summer during periods of unexpectedly high demand. The plants closed because the advent of modern natural gas extraction methods such as hydraulic fracturing (fracking) has made natural gas a much cheaper energy source than coal. Financial advisory firm Lazard reported late last year that a megawatt hour of electricity from coal costs \$60 to \$143, compared to \$48 to \$78 for natural gas.

The coal plant retirements have resulted in a reduction of reserves, which has already had a dramatic impact on summer rates for 2018. Hospitals with contracts expiring in 2018 will have to evaluate the market in depth to mitigate the rise in prices. Long-term impacts, however, are less prevalent for two reasons. The first reason is because the coal-plant closures are quite recent and the impact of these closures has yet to ripple down to affect long-term prices. The second reason is that Texas has had a large surplus of reserves for many years, and a majority of market participants expect the reduced generation to be replaced within a few years, though that could be changing. Very little gas-fired generation has been planned or added to the generation pool to offset the coal-fired plant retirements. Furthermore, despite low gas prices, it is also a difficult time for gas-fired power plants to bring in revenue.

“Prior to the coal plants closing, we had reserves in the neighborhood of 20%,” said Perry Ruthven, managing director of the Houston region for Priority Power, a Midland-based consulting services firm that helps clients manage their energy supplies. “Now, with the loss of the coal plants, we’re at single digit reserves. And there have been no additions to the

generation mix in ERCOT that are expected to elevate reserve margins to ERCOT's minimum reserve margin target of 13.75%."

In addition to declining reserves, energy watchers recognize that summer — the period of Texas' greatest energy usage — is right around the corner. Will the summer of 2018 bring average high temperatures of 88°F or 90°F or something else? Even a small fluctuation in average temperatures can change energy needs dramatically.

"A few degrees on average can have a huge impact on energy use. Summertime is the big mystery," said Ruthven. "Will we have enough electricity generation?" Sustained heat waves vs. occasional temperature spikes can impact energy use, too, according to Ruthven.

Another area of concern is that with such a large percentage of Texas' energy needs being met by one source — natural gas — if anything were to happen to either the supply or the price of gas, the energy market as a whole would be greatly impacted. Wind power is increasingly a factor in supplying the state's energy grid, and solar and nuclear contribute as well, but natural gas provides the lion's share, and a hit to gas production would have significant consequences.

Industry experts in Texas are pondering how reduced production, a shrinking buffer, a narrow energy source, and higher —but unpredictable — summer usage will impact the grid in the coming months.

Hospitals, too, should be paying attention to these seismic shifts in the Texas energy market.

"It's a good time for hospitals to review their energy contracts," says Jeremiah Bastian, senior account executive with Priority Power. "Prices are volatile right now in the short term, but long term rates are very attractive, so it makes sense to be looking forward as far out as hospitals are comfortable."

Bastian says that many of the hospitals Priority Power works with purchased long term contracts in 2016, which, it turns out, was "one of the two lowest points of the market in 20 years." But for those that didn't, now's the time to review contracts, he said.

Even though energy prices have been unusually low for several years, that is likely to change, said Bastian. "We might see more coal plants closing, which will squeeze the market even more."

Additionally, said Bastian, "There can be as much a five times a difference in terms price savings fluctuation when buying gas at one time of year versus another."

Generally, said Bastian, hospitals can often demand better-than-average energy pricing because of the nature of their operations

“In general, hospitals are a coveted load due to high load factor,” said Bastian, senior account executive with Priority Power. “That means that because their electricity use is heavy and consistent, hospitals can demand and get lower rates than some other entities can get.”

But that doesn’t mean hospitals should sit back and relax when it comes to energy acquisition. It’s important that health organizations — for whom energy is a major expense — work with an expert consultant who not only sources the best pricing but understands how timing and risk tolerance factor into energy contracts.

“It’s a very interesting market,” said Bastian. “It’s always changing.”