Centrica in North America

Presentation - London - 6 December 2005

1. Objective and Welcome

Phil Bentley - Group Financial Director

Thank you for coming everyone today. I am glad to see a good turnout of the usual suspects here.

Obviously I think the key today if you look at the North American business, this is a business where we are pretty proud of what we have achieved, but we actually think that we haven't really given the opportunity for the market to fully understand what we are doing and where our plans are taking the business. And if you look at a lot of UK companies that have invested in the States, I think on occasions, certainly in our industry, mistakes have been made. But I think if you look at the presentation today, you will get a chance to meet the guys in the team here, you will see that we have built in our view a very strong business indeed. A business we think can grow well. A business where the team is focused on growth and providing good returns on investments that we have made.

Objective

So today is all about really understanding what is that investment case for North America. We will provide some real detail behind the day to day activities and hopefully give you some sense of how we look at the business and how we look at value in the business. I think this is one of the best teams, certainly other bankers have said this, one of the best utility teams in the North American market and I am very proud of what Deryk and the team have built over the last five years now. Time flies. So on that point, hopefully you will agree with me at the end. I am only here to sort of be the goal keeper for difficult questions on windfall taxes at the end. But we will have plenty of time for Q&A's. It is a North American day and with that let me hand over to Deryk and the team.

2. Background and Strategic Rationale

Deryk King- President and CEO

Phil, thanks for that introduction. We have never been called a Utility Team before. Good morning and thanks for coming today. I am Deryk King. I have been President and Chief Executive Officer of Centrica North America for the past five years. So I would like to start the proceedings by introducing my colleagues from the Direct Energy Leadership Team who are here today.

Firstly I would like to introduce two of our regional Presidents who are here: Bob Huggard, responsible for the Canadian Retail Operations. Bob is also Chief Executive Officer of the Consumers Water Heater Income Fund. And Phil Tonge, who is President of Texas Operations but will also cover other US markets today. We have also got presenting three of our Group's Senior Vice Presidents whose responsibilities span the whole of North America: Maura Clark, Head of Strategy and M&A, Mike Hogan, Head of

Upstream Gas and Power Generation and David Clarke, Chief Financial Officer. And also with us today is Bill Cronin. He is our Chief Operations Officer. Bill is responsible for all energy procurement and trading across North America. In case you are wondering, two Brits, two Canadians, three Americans and I will leave you to guess which is which. You've got their biogs in your pack together with biogs for other members of my leadership team who are not here today.

We have a very full agenda. There is a lot to cover. After my introduction, Maura will paint the current market landscape and then Bob, Phil and Mike in turn will talk about each of the major businesses, Canada, the US and upstream. David will run us through some financial metrics and he will try and provide a number of benchmarks to assist you in the valuation of the various parts of our operations.

Of necessity this is just a snapshot in time in a fast moving environment. So we will also try and anticipate how the business will evolve in the future. We have put aside two sessions for questions.

So let us get an initial orientation by reviewing the scale of Direct Energy. We celebrated our 5th anniversary in North America in August of this year. And in those five years we have grown from three people living in a hotel out of suitcases to over 5,000 employees and we believe we have created a diverse, scale business.

Summary financials

I thought it might be interesting for a change to look at summary financials in our internal reporting currency of Canadian dollars. I am sure you will all know but they are currently trading at just a fraction over two dollars to the pound.

As you can see revenues have grown steadily and we are expecting this year to come in at something in excess of C$7½ billion in revenue. EBITDA grew to C$470 million last year, about £230 million at today's exchange rate, and operating profit as you can see again has grown consistently. First half of this year it was C$200 million. That was up 30% from the same period in 2004. Growth in the second half will be just a tad lower but we still expect to maintain an OP growth rate of around 25% year on year.

The market

So that is all fine, but why on earth are we in North America in the first place? Well it is a matter of scale and opportunity. With regard to scale, we are looking comfortably at the world's largest energy market with aggregate revenues for natural gas, electricity and related services approaching half a trillion US dollars each year. The opportunity is to leverage the skills that we have developed and honed in our UK businesses and transplant our unique energy and services model into this huge American environment.

So let us just go back to scale for a moment. North America has got almost five times the number of households as the UK. As you can see here, power consumption is some eleven times and gas consumption over seven times UK levels. So for example whereas the average UK customer for electricity will spend £307 a year on power, our average customer in Texas will spend over £1,000 a year. Another example: In the last two years alone North America has added more power generation capacity than the entire UK generation fleet.

Geography is also important. North America is much more dispersed than the UK as well as being bigger. There are multiple markets creating a number of risks - regulatory, weather, operations, logistical - that can be mitigated through portfolio ownership in North America. And that diversity of markets also minimises the threat from small and new entrants, because these risks can only be practically managed by large well capitalised and well run firms.

Regulatory landscape

Now to understand our development and our strategy we need to look at a little history. Because almost as soon as my plane landed in North America in late 2000, we were hit by what today we would call a perfect storm of events. We had the California power crisis that had just ended, Enron was heading for bankruptcy, the gas price was starting to become much more volatile and so on.

So it was quickly apparent that our "plan A" which was to roll out a door to door residential energy programme across multiple States and Provinces would not be a viable means of executing on what was an ambitious growth strategy. Fortunately we quickly recognised what was happening in the market place and we anticipated subsequent trends and we have been able to evolve our strategy to counter the adverse elements of those trends, first by focusing more on acquisitions of customer blocks, then advancing our home services market entry plans. Then recognising the attractiveness of incumbent energy positions which led to the AEP and ATCO transactions. Then we moved into larger customer categories and of course now we are building on our upstream asset base as Mike will tell you.

Track record

We are proud of our track record because in just five years we have built a business that is the largest non-utility provider of energy and services in North America. And this has been achieved in what has been a difficult market environment. But we have done it without taking what we think is undue and unnecessary developmental risk and we will talk a little bit more about that.

We have been profitable from day one and our acquisitions have all earned good returns. The business is focused in our view, but sufficiently diverse to reduce the risks of being overly exposed to one jurisdiction or one specific market.

And on the people side you will see from the bios that our management team is extremely experienced. But not just at the top, not just the people you are seeing here today, but also in depth.

And finally we believe we have got a plethora of opportunities to develop this business much further.

Growth through adjacencies

This is a busy slide. I am not going to take you through it, except to say that we have evolved and developed the business through what Bane and Company would call "growth through adjacencies" - a relatively low risk conduit to growth. And it has allowed smooth transfer of skills and progressive build up of our organisational capability. And from our starting point at the bottom left hand corner of this chart in Ontario Gas, we

have by and large developed through single steps of either territorial or product extension.

Pace of development

A significant proportion of our growth has been acquisitive as you know. Here is an executional summary.

- We have carried out more than 20 acquisitions and I have to tell you we have evaluated and rejected a multiple of that number. So we have been very selective in the deals that we have done.
- We have made two divestments, our Georgia Gas business and the flotation and subsequent sell down of 80.1% of the Water Heater assets acquired from Enbridge Services which we put into the Consumers Waterheater Income Fund.
- And we have instigated seven new major organic growth initiatives.
- And finally in 2003 we exited three unprofitable businesses.

So our total gross acquisition spend to date is around £1.6 billion. And if we net off the proceeds from the Georgia Gas customers and the income fund, we have spent just over £1.2 billion net on acquisitions.

Our current businesses

Again here is another busy slide for future reference. I am not going to plough through it, but just talk briefly about what businesses we are in because this is not something that most people have an accurate handle on.

The downstream retail business remains the core of our company in North America and comprises two distinct segments: mass markets and business markets.

Mass markets we define as the business of supplying energy and services to residential and small commercial customers. And small commercial in this context would be for example, a café or dry cleaners. In North America these customers generally fall under residential-type regulation. For clarification, in the UK those small commercial customers are not part of the residential energy business, they are part of British Gas Business. So there is a subtle difference in the way we manage.

North American business market customers, the second segment, are larger, generally in excess of 250,000 kWh or 25,000 therms a year in consumption. And in addition to energy, the suite of services we offer these customers includes performance related energy services, energy management technology and installation, servicing and repair of major heating and cooling equipment.

Downstream businesses are supported by procurement and manufacturing operations in the form of an Energy Management Group which procures all of our energy and our upstream gas and power generation business. EMG, Energy Management Group, also trades in wholesale energy markets. And it manages significant natural gas storage and transportation positions across North America.

Current business footprint

Looking at this a different way, geographically.

Downstream we are organised into three regional units, Canada, Texas and US North. And these regions embrace all of our energy and all of our services for all customer segments, mass markets and business markets.

Energy Management Group operates out of two major centres in Calgary and Houston and its activities are strictly supervised by our risk function. And the management of our risk function reports up an entirely separate management line to Andrew le Poidevin who is Centrica's Chief Risk Officer.

Finally we have our upstream activities: natural gas production in Alberta and power generation in Texas.

We will speak more about all of these businesses during the course of the morning.

Our core strategy – "optimise and grow"

So let me turn to strategy which we review at regular intervals with the Centrica Board.

You may already be getting a sense that the North American opportunity is very large and of course you would not be wrong. So it is extremely important that at Direct Energy our strategy is closely aligned with Group priorities. And currently as you are all aware, our focus as a Group is on the increasing physical and competitive interconnections with mainland Europe. And we intend to participate strongly in both upstream and downstream markets in this space. Our funding requirements for Europe could be very significant. So in the near term that may restrict capital availability for North America. So we are framing our strategy within this Group picture. And we describe the result as optimising growth.

"Optimise" recognises as with any business that you can always improve. And we are intensively focused at the current time on strengthening our operational processes and our core businesses. And that is aimed at enhancing and maximising the returns on the capital that we have already invested in the business.

"Grow" recognises a suite of options with good returns that we can pursue and we can do that largely within our own cash resources in North America.

So if we just look briefly at the components of "optimise and grow", five points:

- One, we will continue to work hard at opening up new residential energy markets. As Maura will tell you, we believe that there are signs that an inflexion point has been reached and passed and that sentiment is moving once again in some states in favour of competitive retail markets. We are absolutely confident that we will succeed in opening up markets over time, but it is going to be a patient game.
- Two, we will continue to build up our home services operations on both sides of the border and we will focus mainly but not exclusively on markets where energy is or will be de-regulated.
- Three, you will hear about the major opportunity in business markets, both energy and services.
- Four, we will continue to support these downstream activities with prudent upstream investments.

- Five, we will continually re-evaluate our cost structure to ensure that it is fit for purpose across all business and functional units, but without of course compromising on our ability to pursue growth.

The total of that constitutes what I would regard as a relatively low investment agenda. But we expect it nevertheless to generate double digit growth in turnover going forwards. And there are lots of options to press the accelerator if we choose to do so.

A strong and integral part of the Centrica group

So we have a profitable, growing business. We earn a positive spread on Centrica's cost of capital as David will show you. We are also a strong contributor to the Centrica Group and we have been and expect to continue to be a significant contributor to both top line and earnings growth in the Group.

We share many common skill sets and I will finish by talking a little bit more about those in a moment.

And of course there is considerable sharing of business models and processes which we cross fertilise through the interchange of people and ideas and networks. And this works both ways. You will spot, you spotted one, you will spot another in a minute, two Brits in our team from North America today. But going the other way, already, Centrica's European Head of Regulatory, Aleck Dadson, started with Direct Energy in Toronto. And many of you also know that British Gas recently poached one of my top executives, Lois Hedg-peth to run its residential energy business.

Over the next few years for the first time we will see a physical linkage between Europe and North America with the globalisation of the LNG business, the Liquefied Natural Gas business and arbitrage between US and European gas prices will be a significant driver of both trade flows and profitability and we are actually seeing examples of this right now. Those players who have the ability and the networks to be able to store, trade and retail gas landside of the regas terminals, instead of just selling ex-ship or ex-terminal, will have a significant competitive advantage.

Next our established position in North America gives us terrific strategic optionality. You heard earlier about how we have modified our strategy as events have unfolded. But we have demonstrated our ability to react quickly to those. We have a proven execution track record of dealing with change.

And then a key attribute that sets us apart from all of our smaller and many of our larger competitors in North America is Centrica's strong credit rating and this underpins commodity procurement and trading without undue recourse to more expensive credit support mechanisms. And finally of course North America diversifies Centrica regulatory and market risk.

Overall our view is that this is a strong slate of benefit that ties Centrica's operations in the UK and North America together in a way that enhances both operations.

Synergies with Centrica in the UK

So let me just finish by going back to the point about common skill sets.

You would expect of course that companies in the same business would share common skills and processes. And of course that is right. But I am not sure if it is fully appreciated just how many of our UK skills translate into the North American environment. And here are some examples about which my colleagues will talk later. But as with people, it is absolutely not appreciated how important or the extent to which skills flow the other way. And I would just like to highlight three examples.

- Firstly product design. Many of the novel energy products that British Gas is currently launching have their roots in the fixed and capped price products that we have been selling in North America and hedging in North America for the last five years.

- Secondly, we are one of the leading edge developers of coal bed methane in Alberta. And those leading edge skills that we have are increasingly being called upon to evaluate opportunities in what in the UK is just a fledgling business.

- And finally as you will hear from Bob, there are exciting opportunities to roll out the automation and energy management technologies that are part of our Canadian business market's operation, into the large British Gas Business customer base.

So skills transfer is increasingly a two way street and my team works very closely with their UK counterparts to ensure maximum benefit for the Group.

So that is my introduction. I hope that sets the stage for what you will find interesting presentations from my colleagues and I would now like to hand over to Maura Clark who will bring us up to speed on the North American market environment.

3. Regulation and Competition

Maura Clark - Senior Vice-President and Head of Strategy

Thanks Deryk and good morning. I would like to start by just reviewing some of the high level trends that we are seeing in both the regulatory and competitive landscape as all of these things form an important backdrop to our business.

Regulatory and competitive landscape

You were reminded earlier in Deryk's presentation about some of the events that initially put the brakes on deregulation in certain jurisdictions. However as I hope you will hear today, we believe that the days of doom and gloom are generally gone and we are starting to see some encouraging signs that the slow but steady march towards retail competition is progressing.

Except for the handful of States that rescinded legislation prior to market opening there have really been no successful attempts at reregulation and we have seen a recent win for pro-competitive forces in the voting down of Proposition 80 in California recently. We are currently seeing a strong lobby for the continued development of retail markets in North America and in almost all of the markets have seen increased migration levels in the last few years.

Texas continues to be recognised as the most successful retail electric model in North America and since the market opened in 2002 close to 60% of total residential and commercial & industrial load have switched to competitive suppliers. Over 50

competitive retailers are actively operating in the Texas market. Texas will be transitioning through its next phase of deregulation as the Price to Beat mechanism is phased out at the end of next year. But you will hear from Phil Tonge in a few moments what we expect to see in that next phase of deregulation.

In Canada we have encountered some setbacks in our key markets, but we are currently enjoying strong sales in a newly opened electric market in Ontario. But in residential markets generally we expect further opportunities to be somewhat limited while energy policy makers focus on developing the business market space. A notable exception is the New York market which we expect to be entering early next year.

Recent high and volatile commodity prices have tested us along with many other retailers, but we are pleased to be able to say that with our conservative hedging policies, the optionality of our upstream gas and power positions and the very solid capability within our Energy Management Group, that we have weathered the storm extremely well. We are actually finding that these current market dynamics are helping us sell our fixed price proposition as our customers look for price certainty.

In terms of our competitive landscape, a dominant theme for us has been the fierce competition for physical assets by financial sponsors, hedge funds and tax advantage structures. And we have been very careful throughout this environment to maintain our financial discipline and we are committed to ensuring appropriate long run returns in our acquisitions.

A key legislative development this year was the signing into law of the US Energy Policy Act, which was generally neutral to supportive for retail competition. The Act included the repeal of the Public Utility Holding Company Act which eliminated a number of obstacles to utility company mergers. So more consolidation activity and potentially new entrants to the space are all predicted. But it is important to understand that some of the key impediments and some of the traditional impediments to utility consolidation still remain.

With the repeal of PUHCA, utilities now also have more flexibility to pursue unregulated activities but the track record of utilities in this regard has been extremely poor and we don’t really expect any significant threat to our model from that camp.

So in summary, while the environment is often challenging we are thriving against this backdrop and we are actually seeing some very positive momentum in the market broadly.

Restructuring in North America

We thought it would be helpful to highlight some of the key attributes of the North American regulatory environment.

In North America unlike the UK there is really no single body driving deregulation. The primary influences are provincial and state legislators and regulators. This results in a very fragmented market where opportunities differ widely between States and even within States. This lack of uniformity complicates the operating environment and requires constant monitoring to stay abreast of regulatory changes. Changes and rules can rapidly create opportunities for which we have to be and have been ready. This complexity plays to our strengths and actually constitutes a barrier to entry. Our team

of regulatory professionals has successfully managed and driven change in both our existing and target markets. Typically we are much more nimble and responsive to opportunity than the incumbent utilities.

Unlike the UK as well, the US regulators are often more focused on protecting the customer rather than fostering choice. And there has been a lot of debate recently around the benefits of choice for small customers. However we have recently seen some credible industry participants come forward with very strong evidence supporting the merits of deregulation. According to industry consultants Cambridge Energy, retail customers have saved some $34 billion between 1997 and 2004, relative to their projection of energy costs without restructuring. And in Texas the Public Utilities Commission reported savings of over $1.5 billion in just one year of competition. These are not insignificant amounts.

So in summary, while we are cautiously optimistic about continued improvements in our regulatory landscape, we expect most if not all of the momentum to continue to be in the commercial and industrial space. And to be very clear, the mass market growth that we are outlining today is not predicated on any expected improvements in the regulatory structure. If that happens it will simply be an upside.

Gas regulatory landscape

Let's take a closer look at the regulatory landscape. Here is a map of North America which indicates which natural gas markets are currently open and to which customer segment. Deregulation of the gas markets began in the 1980s and the market is mature with a very liquid wholesale market. You can see that the large C&I segment is open to competition across all states and provinces, although the residential opportunities are somewhat more limited. Partially open markets occur when State legislation has required development of competitive markets, but where not all of the utilities within that State have complied.

And it is very important to note that just because a market is technically open does not mean it is economic to do business there. Rate caps and default service for example can result in limited headroom. And this dynamic is particularly important in North America where a primary competitor is the incumbent utility. We are very diligent prior to entering a market about assessing this and other dimensions of the market's prospects before we make the step to invest in that region.

Electricity regulatory landscape

The electric market is somewhat less mature as restructuring began only in the 1990s. The transmission network still remains somewhat fragmented and regional transmission organisations and independent system operators are still evolving. Liquidity in the wholesale markets is generally good, but it varies between regions and is limited in some areas. But generally the market is progressing well. Flawed retail models are slowly being replaced by more appropriate market based pricing structures.

One of the regions that has moved substantially in the right direction for competition is the North East US. This represents a huge opportunity for us to leverage our existing skills and footprint. The population of this area is close to 50% of the entire US population with total load estimated about 1,000 TWh, so three times that of the UK. The added advantage of focusing in the North East for us is that these markets are also

open for gas, so therefore offer dual fuel opportunity and product bundling opportunities as well as operational efficiencies.

We entered the power business markets in both the North East and the Mid-Atlantic this year ad we are planning on entering the New York market in early 2006. New York is an attractive market that offers a lot of pro-competitive mechanisms such as migration incentives and purchase of receivables.

Switched volumes

I mentioned earlier that switching was still proceeding at a good pace. This graph illustrates that switched volumes in the US are approaching the total UK power market load. Industry consultants are predicting total switched load of 500 TWh by 2010. The majority of this predicted new volume is expected to come from the US North East. One notable exception is California. California is not currently on our agenda but we will continue to maintain a watching brief on the developments there.

Regulatory status in our core markets

Let's have a closer look at the regulatory status in each of our core markets.

In Ontario the evolution of regulation has been somewhat stop-go. Following closure of the small customer electric market in 2002 the provincial government reopened the market this year after what was a vigorous effort by our regulatory team which involved several high level meetings between Deryk and senior government officials. But unfortunately the Ontario government continues to subsidise a regulated tariff structure at below wholesale costs. This tariff is expected over time to migrate to fully cost reflective levels and in the meantime our fixed price offering is selling extremely well even at a substantial premium to this regulated tariff.

An important consequence of market reopening is that we will encounter some pressure on Ontario electricity margins in '06 and '07 as we cease to benefit from provincial rebates and as we incur customer acquisition costs for the first time in three years as we start to grow that business once again. And Bob will explain in a little more detail how we are approaching this opportunity, but suffice it to say we are extremely excited about being able to market dual fuel products in Ontario.

In Alberta the provincial government continues to wobble in the face of high and volatile commodity prices. They have responded by funding new programmes which provide rebates against gas prices and by interfering in the retail power market by delaying the full force of wholesale cost pass through. And as a result customers see less benefit in signing fixed price contracts and migration to unregulated supply has been slower than we would have expected. You will also hear from Bob later on how we are dealing with this.

The Texas market continues to function extremely well and we are very happy with the business we have there. Phil will explain how we plan to manage through the expiry of the Price to Beat mechanism, but the bottom line is that we expect market participants to behave rationally and as a result margins should hold up very well. The Texas market and regulatory structure was really tested this fall with the hurricanes and the resultant high gas and power prices. And it is noteworthy that during this period of unprecedented dislocation, each of the large retail competitors worked with the Public

Utilities Commission to ensure that retail customers were not disadvantaged. And the market structure remained intact in spite of significant political pressure to intervene.

And finally in the North East we are encouraged by the business market prospects and the New York dual fuel opportunity in both business and residential markets.

Competitive peers

Let's turn now briefly to the competitive landscape. We tend to think about our competitor universe across our various business segments since there is really no one true peer company that operates in all of our markets or businesses. It is an important observation that we really have a unique model with our presence in both business and residential markets. We believe our portfolio of businesses confers a real advantage. For example our geographic footprint provides both weather and regulatory diversification. Our broad customer base with different load factors allows flexibility in energy procurement and risk diversification. And the combination of energy and services targeted to a range of customers is also unique to us.

So we are generally forced to look at our competitors across business segments, segmented again for geography. In residential and commercial & industrial markets we see a lot of competition in both of those areas and in both of these markets we often compete against utility pricing that does not always represent the true cost of supply.

In Canada we have leading market positions in Ontario and Alberta, the two markets that are open to competitive retail suppliers in all sectors. In Texas we have a strong number three position in a very large market with good growth upside. We often see other insurgents in our markets. However recent high commodity prices are causing distress to some of the smaller players and we expect to see a fall out of some of the less well capitalised players in the near future.

In business markets Constellation New Energy is the market leader having achieved very rapid growth and significant market share since its entry into the market by a large acquisition in 2002. We are somewhat of a late entrant to this segment, but we are seeing very good growth with first half '05 power volumes up 80% and gas volumes up over 50% over the same period last year. And while Constellation is dominant on a multi-regional scale, we believe there is plenty of room for additional players and we expect to be able to achieve our growth targets and achieve acceptable returns.

The home services base is highly fragmented and still very dominated by "Mom and Pop" ventures in many areas. We are rolling out a strong business across Canada, based on a platform created by our Enbridge acquisition and in the US by the RSG acquisition. Two large service companies, Service Master and Service Experts, have large but very geographically dispersed operations that don't represent a material threat in any of our core markets. There are many examples of failed rollups in this space and through our disciplined model of organic growth, supported by tuck-in acquisitions, we will avoid the traditional pitfalls.

In business services and technology we believe we have somewhat of a unique model which carves out an interesting position where we don't really need to compete head to head with the large equipment manufacturers to be successful. Importantly for services there really are no material competitors offering bundled energy and service products

with the credibility to deliver and as such we are very excited about the prospects for this business.

So in summary, while we have a healthy respect for our competition we are very confident that we will continue to succeed. We have a unique business model and the capabilities required to thrive in our regulatory and market landscape.

I would now like to hand it over to Bob Huggard who will review the Canadian business with you.

4. Canadian Retail Operations

Bob Huggard - President Canadian Retail Operation

Our Canadian retail operations are comprised of residential and commercial energy businesses focused in Ontario and Alberta which we call mass markets, our leading home service business in Ontario and growing operations in Manitoba and Alberta, and business or commercial energy and services customers nationwide which we refer to as Business Markets.

Mass markets energy

Let me start by talking about our residential energy business. I would like to lead off with some key facts about our Canadian residential and small commercial energy businesses.

As we mentioned earlier, mass markets is mostly residential, but also includes some commercial who consume up to six times the volume of the residential customer. Our Ontario business has a share of just under 60% of the switched gas market and about two thirds of the switched power market. Most of our Ontario customers are on multi-year, fixed price contracts. In Alberta we have an 80% share of the gas market and 13% of the power market. Our customers in Alberta are predominantly on a regulated pass-through rate. But we are progressively switching them to competitive offers. I will discuss this situation in more detail later.

In Ontario the regulatory backdrop on the gas side has generally supported a high level of competitive activity although power markets have presented greater regulatory challenges. After three years of below market-price caps, the Ontario power market is edging towards rates that reflect the true cost of power. This transition is working in our favour creating strong interest in fixed price offers. Our propositions focus on helping customers limit their exposure to rising or volatile commodity prices, generally translating into five year fixed price supply contracts for both power and gas. These contracts are fully hedged.

Risk is also reduced by invoicing for our products on the utilities bill, very cost effective and with the utility carrying the ad debt risk.

In aggregate the combined regulated and deregulated gas and power businesses produced an operating margin of 3.2% for the twelve months ending June 30 2005. We are forecasting growth, growing operating margin to 4-5% in mass markets.

Direct Energy's proposition emphasises price stability

Here is an example of a mailer that we distributed earlier this year to mass market customers promoting our natural gas offer. Our marketing materials reinforce the long term price stability proposition by educating customers about historic price trends and demonstrating the savings realised by past customers. Ancillary features of the market reinforce this long term proposition and help support the economics of this product. Customer mobility is limited with liquidated damages on contracts acting as a deterrent. Evergreen contract renewals are permitted. Cost to serve is reduced as billing is done through the regulated T&D company. And customers call for service on average less than twice during their five year contracts.

Fixed price proposition

The chart you see on this slide highlights the positive benefits of our mass markets fixed price promotion for a five year customer.

Unlike the UK we continue to face competition from utility regulated prices in some markets. The so called default service in Canadian gas markets is priced as a wholesale cost pass-through, with rates being reset at various intervals; monthly in Alberta and quarterly in Ontario. Consumers have been more shielded from the true cost of power than they have for gas, with retail prices typically being set at a discount to the prevailing spot market. However programmes are under way in both Ontario and Alberta to gradually increase consumer exposure to market prices. We are particularly optimistic about the Ontario opportunity as you will see shortly.

So in contrast to the situation in Texas that Phil Tonge will walk you through after the break, there is no built in headroom in Canada. Accordingly our offers are focused on providing consumers with long term price stability, much like the value proposition of a fixed rate home mortgage. We don't promise savings, however given rising prices over the past few years, the fixed price proposition has allowed the average Direct Energy customer to save nearly C$1,000 during the five year term of their contact, as illustrated in this chart.

The long term fixed price offer is well established in the Ontario market with nearly half of all households on fixed price contracts. However interest has reached a new level in recent months as news of historically high gas prices has been quite prominent in the public eye. Our newer step-down product offering a one cent per cubic metre reduction in price for each year the customer stays with us is resonating well in this environment, particularly among customers wary of locking in at the peak.

Evolving channels

Staying with mass markets, a key part of our strategy to grow our Ontario gas business is to diversify our sales channel mix away from its predominantly door to door legacy. The "Energize" programme which engages service engineers in the energy sale, has been a cornerstone of this effort. Engineers have been trained to present the fixed price energy proposition to customers upon completion of a successful service interaction. Their efforts contributed 17% of gas sales year to date in 2005. This approach offers significant advantage to an insurgent energy marketer, particularly in a utility-billed environment because it provides a tangible representation of the company that is tremendously important. 79% of consumers report an awareness of Direct Energy compared to 32% for our closest competitor. We attribute this disparity in large

measure to our over 500 branded service trucks on the road and over 670,000 service visits we perform each year.

The productivity of our telemarketing channel reinforces the synergy between the services and energy segments of the business. Sales per hour for calls made to protection plan customers are nearly double that of non customers. And inbound calls come primarily from our core home services territories.

Affinity programmes represent another growing channel. For example, our recent offer of five hours of free long distance calls each month to customers who either sign or renew their energy contracts has been a huge success.

Door to door of course will remain an important part of our channel mix and accordingly we have also invested significant resources improving its effectiveness, focusing on agent training certification and compliance.

Expiry of the rebate in Ontario

I want to say a few words now to amplify Maura's earlier comments about the changing electricity landscape in Ontario as it applies to mass markets.

Following the opening of the power market earlier this year, 2006 will mark the end of compensatory payments that we have been receiving from the Ontario Government under what is known as the Market Power Mitigation Agreement. The MPMA was put in place between the Ontario Government and Ontario Power Generation, the government controlled entity which owns the lion's share of generation in the province. Under the agreement, OPG was directed to rebate profits from generation above a pre-set amount. These excess profits have been returned through the MPMA rebate and Direct Energy has been receiving payments during this period. The payments will cease in April 2006 as expected and gross margins on our residential power book will thus revert to lower, but still attractive levels.

Going forward we believe the reopened power market will support sustainable gross margins in the neighbourhood of at least 13%. While this contribution level would appear uneconomic in Texas and in the UK, utility billing, the absence of bad debt risk and contractually assured low attrition rates allow it to be attractive in Ontario, particularly in light of the dual fuel opportunity with gas.

Alberta

I would now like to turn your attention to western Canada and our purchase of the ATCO retail business in Alberta. This £37.5 million acquisition gave us one million regulated gas and power customers in Canada's second largest and fastest growing market and the incumbent utility billing envelope. This has allowed us to establish the Direct Energy brand at a low cost in a very short period of time with today an 81% recognition rate.

The business comprises two segments, Direct Energy Regulated Services and Direct Energy Essential Services. The regulated business operates primarily on a pass-through basis, although we earn a small operating margin on electricity hedging. The unregulated business competes with such pass-through economics but is able to charge a premium for stable prices. However continued meddling by the provincial government with the rules has discouraged customers from switching which has been lower than

anticipated. There has also been a reluctance to allow the use of telemarketing as a sales channel, although we continue to press strongly on this front.

Our forward perspective is that in the near term, switching will continue to be slow and this will be a patient game. Consequently we have reorganised our Calgary based operations and reduced our cost base significantly. However residential energy was only one aspect of the ATCO retail investment case and business markets and home services opportunities remain intact. We are now focused on accelerating the growth of these businesses and on expanding our presence in neighbouring British Columbia.

Canada Home Services

Turning to home services, Direct Energy Essential Home Services currently serves more than 1.8 million customers, representing over 40% of the households in Ontario and over two thirds of households in areas we serve.

We offer the service and replacement of the primary energy consuming elements of the home, specifically;

- the sale and installation of heating and air conditioning systems for homes
- the installation and rental of gas fired water heaters
- a range of service and maintenance protection plans for key elements of the home infrastructure, notably furnaces, air conditioning and plumbing and drains.

The home services businesses acquired from Enbridge in 2002 has grown strongly but remains largely focused in the greater Toronto area. Expanding into the neighbouring territory is a key focus at this time and will represent nearly a doubling of our addressable market.

Our home services focus in Canada is very much aligned with the model that has been successful in the UK and there has been extensive knowledge and management transfer between the two operations. Whilst certainly a younger and smaller scale business, the model is working well in North America.

This growth of high contribution margin customers combined with the completion of our efforts to leverage our transformed platform and ongoing optimisation of our cost structure is expected to produce high single digit increase in turnover and a substantial improvement in operating margin over the next years.

You will see that we are targeting operating margins of 14-16% in this business, but need to understand that this comprises margins of approximately 10% in our protection plan business, boosted by higher operating margins from our shareholding in the Income Fund.

Restructuring of Enbridge Services

As I mentioned, the Ontario home services business we operate today has evolved from the business that we acquired from Enbridge in May 2002. The acquisition was predicated on a three legged strategy for future value creation: Restructure, Transform and Grow.

First we spun off the portfolio of rental water heaters into a publicly traded income trust, the Consumers Waterheater Income Fund, in a transaction that created net

proceeds of about C$856 million after sell-down. This left us with our present 19.9% share, the quoted market value of which was just shy of C$160 million or £80 million as at November 29th. And left us also with a loan book worth over C$100 million.

All in all this restructuring process left us with a leading home services capability in Ontario plus 95,000 unregulated gas customers for roughly minus C$100 million. The spin off included an agreement whereby Direct Energy receives 35% of the waterheater rental revenue stream in exchange for servicing the tanks as needed. This revenue stream is tantamount to having protection plan contracts covering the 1.3 million tanks and should be distinguished from the 19.9% equity share we receive from the Trust's stand alone earnings.

Knowledge transfer from British Gas

Second, we leveraged our UK home services experience and transformed the business, creating a platform with sufficient scale to support growing contract volumes and expansion into product adjacencies. This included the closure of district offices, deployment of new systems and consolidation of activity in central locations to capture economies of scale. Our platform investments have included a number of initiatives aimed at strengthening our scheduling capabilities. Specifically we now have wireless systems in all of our trucks and are thus able to track technician availability in real time.

Third we leverage the utility legacy and our energy customer relationships to substantially grow the business. What was a repair-focused business with 320,000 breakdown protection plan customers has grown by 60% to date.

We have also seen expanded revenues per customer by upselling to maintenance plans and launched plumbing and drain and whole home cover.

The business currently employs 780 heating, ventilating and air conditioning – or HVAC - service technicians and installers across the corporate and franchisee operations. We believe this is the largest repository of these skills in the country. And we are widely recognised as an employer of choice in the industry. The performance improvements reflected in the charts here testify to our success and we are already leveraging the platform and expertise to accelerate our expansion in Alberta and Manitoba.

Leading position in Ontario Services

You are all familiar with the strategies and products offered by British Gas Services here in the UK. We are replicating these programmes in Canada with the one exception being the rental programme. Rental waterheaters represent our most stable and highest margin revenue stream. Waterheater rental is a very entrenched behaviour in Ontario having been initiated by the incumbent gas utilities in the 1950s in an effort to create stable demand for natural gas. At present roughly 85% of households in the province have a rental tank. The proposition is predicated on replacing an up front capital investment with a low monthly rental fee which includes the repair or replacement of the tank at such time as it is needed. So think of it as coverage for water heaters.

Business Markets

Let me switch finally to the business market sector. As discussed earlier, deregulation of commercial and industrial markets, C&I, is progressing in a number of North American regions. We are well positioned to capitalise on this growth opportunity in the market.

In Canada, Direct Energy had a small business markets gas operation in Ontario at the time of acquisition in 2000. Since then we have expanded into electricity and become established in British Columbia and Alberta. Our Canadian Business Markets organisation embraces both energy and services which I will come to in a minute. We have now grown Business Markets in Canada to a £200 million business, equivalent in volume terms to over 400,000 residential customer equivalents. Although our pace of growth and a backwardated gas curve have impacted operating profitability over the last 12 months we are laying the foundation to be a strong player in the sector.

The current backwardated curve which compresses margins in the short term and our expensing of all cost to acquire costs incurred (although they support the sale of long term contracts) presents a conservative OP margin.

We are forecasting continued top line growth of between 15-20% per annum with sustainable operating margins in the range of 3-4% once the hectic pace of growth ends.

Business markets strategy

Our strategy for business markets in Canada is built on two aspects of differentiation from our competitors:

Firstly we are focusing in on mid-sized C&I energy customers generally between 250,000 and 10 million kWh of annual power usage and between 25,000 and 1 billion therms of annual gas consumption. Customers with this level of consumption are above the threshold covered by mass market tariffs, but below the consumption level at which wholesale procurement is pursued.

Secondly we have developed a unique energy related services and technology capability, a natural adjacency to the gas and electricity needs of our customers through the integration of the nationwide mechanical services capabilities acquired as part of Enbridge Services in 2002. The subsequent farm-in of the integrated building technologies, building automation and control business, a number of small infill technology acquisitions and ongoing in-house product development that has expanded our offer to include proprietary energy information systems technology. These service and technology capabilities integrated with performance contracting and our core energy retail business combine to form a differentiated total energy solution with the ability to manage customer energy requirements on both sides of the meter.

We will exploit the broader and deeper customer relationship created through our model to drive the margins necessary to earn an appropriate return on the capital employed in the business with target post tax returns in the mid teens.

Total solutions approach

The advent of new and lower costs demand reducing technologies aimed at business customers is increasing demand for service and technology solutions. Improving economics, buoyed by increasing commodity costs, is also serving to expand the market to lower consumption segments. Additionally, demand reduction technologies are now

being integrated with real time, supply side market information to realise even greater savings. As this convergence materialises, energy service providers with the capability to manage both sides of the meter will be naturally advantaged.

Direct Energy's total solution approach demystifies the energy management value proposition and stimulates incremental switching. In addition to increasing the size of our addressable market this focus on new switchers effectively reduces competitive intensity we face in bidding for individual contracts.

Growing success

Since creating Business Markets we have developed strong customer successes. The combination of our dual fuel capabilities, cross regional energy footprint and national services capabilities have made us a supplier of choice for many blue chip customers in the Canadian market.

Examples here include the Corel Centre, a major sports venue; Marriott hotels; a leading department store;Big-Box format retailers with a presence across North American; Tim Hortons, one of the largest Canadian restaurant chains with thousands of locations coast to coast; and the University of Calgary where we are implementing a seven year, C$300 million energy and infrastructure contract.

Our unique ability to help customers manage energy costs both through optimal procurement and demand side management have enabled us to integrate and win key commodity contracts. Sears is an example, where we have integrated demand response and load curtailment building technologies with real time energy price exposure. These high profile relationships have established our credibility as a leader in serving the converging energy and services market.

Growth opportunity

Whilst the regulatory pressures in mass markets have limited immediate growth potential, business markets still represent a material growth opportunity for our Canadian business. Of the total open and eligible Canadian C&I market of 20 billion therms and 150 TWh, Direct Energy has less than 5% market share.

These markets are highly fragmented across the provinces shown on the chart with incumbent utilities maintaining significant unswitched load, especially amongst the smaller consuming C&I customers in our target market. These customers' energy needs are under-managed and under-served and the current high priced and volatile market environment has released a pent up interest in what we have to offer.

Canada Retail summary

Summarising: whilst Direct Energy is already a leader in most of its Canadian operations, substantial opportunities remain to increase operating profit.

In residential energy we see substantial upside from starting once again to grow our electricity business in Ontario, leveraging our leading share of the competitive gas market with dual fuel offers. Increased sales focus in the under-penetrated regions along with continued channel diversification and customer segmentation in core areas will drive further share gains in both energy and services.

In Alberta, despite regulatory set-backs in the residential energy market, we will create value from the acquired Alberta business by accelerating services and business markets growth. This business provides a western anchor for our national capabilities, a key factor in serving commercial customers.

In the business space our total energy solutions capability and national coverage on services will enable continued rapid expansion.

And with the Direct Energy brand now well established and critical mass gained, we are now in a position to significantly improve our cost structure. To that end we are planning a significant cost reduction programme over the next three years. This combined with the top line growth opportunities outlined above, should result in substantial OP growth contribution to the Group.

5. United States Retail Operations

Phil Tonge - President Texas Retail Operation

My name is Phil Tonge and I am with the Texas Retail Operations and I am going to spend the next few minutes talking about the US.

Our current US business portfolio is primarily centred in Texas along with the North East and Mid West regions. With the acquisition last year of the Residential Services Group we also have a growing home services and residential new construction business with operation in ten States with the largest footprint being in Texas. I will talk more about each of these.

US Retail agenda

Our US retail strategy has both residential and commercial dimensions and includes energy and services propositions.

The geographic focus of residential operations is determined largely by regulatory conditions. Prospects are good in Texas power and Ohio gas and a large dual fuel opportunity is emerging in New York.

Residential energy positions in these States will be supported by an expanded heating, ventilation and air conditioning or HVAC services operation, both in the residential new construction and existing home markets, leveraging the platform we acquired with RSG last year. We are refining the model in Texas and will migrate it to other markets as appropriate.

Business Markets energy in the north east will be the dominant growth engine over the next few years. As with our residential growth strategy, in the business market space we will strive to deepen relationships with our customers by offering a comprehensive suite of energy related products and services.

Of course all of these efforts will be underpinned by an ongoing focus on leveraging our highly developed regulatory capabilities to advocate for policies that support our objectives.

Texas

Now onto Texas. Texas is the second largest energy market in the US. It has a current population of 23 million and is expected to continue the plus 20% growth rate experienced in the prior decade. The State has a legacy of fostering competitive markets as witnessed by the broad support for energy deregulation and its leadership in the deregulation of the local and long distance telephony markets which are widely regarded as successes.

The Texas competitive market is comprised of five service territories shown here on the map. The incumbent retailers are shown. In blue we have CPL and WTU, which are our incumbent retail businesses. TXU, Reliant and First Choice Power. In addition to the incumbents as Maura mentioned earlier, there are numerous competitive retailers in the State who are unaffiliated with an incumbent retailer. As you can see from the blue patches on the map our CPL and WTU territory is widely dispersed across the State. It actually covers an area larger than the UK. The area is predominantly rural with fast growing pockets along the Mexican border. The customer base there is heavily weighted toward residential users, more heavily weighted than other territories are.

We commenced marketing in TXU and Reliant territories in 2002. These regions offer tremendous opportunities for our insurgent marketing efforts. They are located in densely populated urban areas with a large proportion of commercial customers and they have approximately four times the number of customer opportunities as we have in our incumbent territory.

All in all our presence in Texas offers access to an addressable market of five million households.

Texas residential energy

I would like to walk you through some of the key highlights of Direct Energy's Texas mass markets energy business. The business produced turnover in excess of £800 million for the twelve months ending June 2005, representing 12.9 TWh of power consumed by roughly 900,000 customers. And it is a substantial contributor to the total North American profits with a healthy operating margin of 9%.

Our Texas operations are a balanced portfolio of incumbent and insurgent customers that effectively leverage the opportunities inherent in this competitive market structure. Our incumbent customer base makes up about two thirds of that portfolio today and as I mentioned is approximately 80% residential.

We grew our organic business by 53% in 2004 and have continued that pace in 2005. And we have outstripped our major competitors in terms of organic growth in each of the last four quarters.

Finally the RSG acquisition has given us a home services platform to support our insurgent marketing and retention efforts in Dallas and Houston. Going forward our priority will be to expand this capability to our incumbent CPL and WTU territories.

Texas mass markets strategy

Our mass market strategy in Texas is simple; build on our strong number three position and narrow the gap with our two key competitors by outperforming them on retaining incumbent customers and acquiring new insurgent customers at a faster pace while meeting our profit commitments. This will necessitate a sharp focus on managing through the volatile commodity pricing landscape that we have been through and maximising the potential opportunity associated with the expiration of the Price to Beat or PtB rules at the end of 2006. Maura mentioned this briefly and I will expand more on it. We have already demonstrated our ability to do this. We have been purchasing forward prudently and we have been investing to increase our procurement flexibility.

Our strategy will be underscored by a constant focus on operational excellence to ensure that we are creating maximum long term value with our growth efforts. We are placing particular focus on reducing our cost to acquire (or CTA) and our cost to serve (CTS) which are key to achieving profitable growth in our insurgent territories. We achieved 31% reduction in cost to acquire and 18% in cost to serve in 2005 and expect continued decline in 2006. Finally, modest acquisitions will likely play into our growth plans both to accelerate our growth in energy and to expand our home services coverage across the CPL and WTU territory.

Price to Beat

One of the most important features of the Texas market is the built in headroom included in the default service tariff known as the Price to Beat or the PtB as we call it. This is the rate against which all insurgents must compete for customers and it was designed to allow sufficient headroom and transparency for insurgents to offer material discounts to consumers. Certain specific provisions of the PtB mechanism bear mention:

- The rate setting mechanism mandates that the PtB fuel charge to be set based on the 20-day moving average of the NYMEX strip price for natural gas.
- The timing of when rate increases are filed are at the retailers discretion, subject to the restriction that rates may only change twice a year.
- When the market first deregulated in 2002 incumbents were only permitted to offer the Price to Beat rate to their customers. Beginning this year however we were given the flexibility to add other rate plans in addition to the Price to Beat. In January 2007 the Price to Beat rate requirements are scheduled to go away entirely, at which time all pricing will be determined by the market. We are advocating for the Public Utility Commission to proceed with this plan and based on our 2005 experience believe that this event will not materially impact the margins that we are able to achieve on this incumbent business.

For legacy reasons related to the stranded generation and higher transmission costs, our Price to Beat rates have generally been higher in the CP&L and WTU territories. This stimulated higher market switching in our territories at market opening but we have since implemented numerous strategies to mitigate the churn and I will talk a bit more about that.

Customer proposition

Now this looks like a blank chart. In our organic business we have had success by offering a value proposition that includes a guaranteed percentage savings off the incumbent Price to Beat rate. We have not taken a position of being the lowest priced alternative and instead we have focused our efforts on being good overall value with our

service and financial stability as part of the package. At the same time, we know directly from our competitors, we have shaken up the market a bit with some innovative and award winning campaigns. And the advert you are about to see won a Bronze Lion Award at Cannes and has been very successful in raising awareness of Direct Energy and its offers in the marketplace.

[Run advert]

Sales performance

Our residential distribution channels consisted of door to door and outbound telemarketing until the second half of 2004. Since then we have greatly diversified by adding mail, the direct response TV ad that you just saw - and we have a family of those that all have the same theme as they have been raising their prices quite frequently. We use associations now and we have also added kiosks to the mix. Beyond these conventional approaches we are also forming alliances with builders with whom we have relationships through the acquisition of RSG. The typical agreement we have is predicated on a mix of the builder's commercial business and the residential business. I will spend a bit more time on this when we discuss RSG.

We are also evolving what we call our "Biz Perks" programme which provides incentives to the employees of our business customers to enrol with Direct Energy for their residential supply. These initiatives as I have mentioned have already produced a 30% reduction in costs to acquire year to date and we will continue our diversification efforts to drive our CTA down and to reach the highest value customers.

Sales

Our strategy in Texas is to maximise total net growth of our incumbent and our insurgent businesses. We are focusing our sales and retention efforts on higher value customers and tailoring our channels, messages and our product offerings accordingly.

The next few slides will demonstrate our recent successes in this objective and is made more significant we believe by the fact that we have outperformed our larger more established peers over the past twelve months.

We have made tremendous strides during the past year in building sales momentum in our insurgent business. We think this is primarily attributable to a few things:

- First we have an easy to message lead offer: guaranteed savings, easy for residential customers to understand.

- We have made a brand commitment: our Texas operation utilised three different brand names sequentially during our first two years in the market. Our commitment to the Direct Energy brand for the last two years has begun to pay dividends. Our partnerships with such strong local brands as the Dallas Cowboys and the Houston Rockets sports teams along with a multitude of local events have combined to make Direct Energy a known and trusted name across the State.

- Another factor is that we use channels to capitalise on the mobility of Texans who move at a rate of nearly 20% per year. Our focus on the highly mobile multi-family or apartment segment of the market has been a significant source of customer

growth. In this segment we flow power to the property managers, vacant units and common areas, regardless of a specific tenant's choice of supplier. Then the property manager acts as a low cost distribution channel or sales agent, signing up tenants at the time of moving.

- Our home services business acquired just over a year ago is beginning to contribute to growth in our energy business. We are pleased with our progress to date and I will spend a bit more time on this as well when I talk about RSG.

- Finally as a point of context, commodity price trends do play a role in driving overall consumer interest in the energy purchase decision. As a result switching was particularly active in this past third quarter with high summer bills acting as the catalyst for the interest, spurred on by a little bit of aggressive competitive marketing.

Attrition

A critical part of our overall growth strategy has been to stem the attrition in our incumbent territories as we have increased the size of our organic base.

Despite increased prices and greater headroom in our CPL and WTU territories, attrition in our incumbent business has slowed dramatically. It is at the lowest rate since market opened. And we believe this is due to some of the pioneering efforts we took to retain customers.

- We were the first incumbent to offer a rebate programme, offering a bottom line percentage discount in peak usage months of June, July and August to offset the impact of increases in the Price to Beat rate.
- We have offered price stability to our customers by guaranteeing there will be no further increases in the Price to Beat for a period of eight months through June of 2006.
- We have extended for six months the low income discount programme that was discontinued by the State of Texas at the end of August 2005. We have been an active contributor to social agencies to provide assistance to support low income customers who are unable to pay their electricity bills.
- We have made investments in improved sales and service practices that have resulted in a 74% reduction in the public utilities complaints between 2003 and 2005. That is a direct driver of customer attrition.

It is also worth noting here that we have completely resolved any early issues we have had with the execution of unauthorised switches and our reputation both with regulators and the public has improved tremendously. As a result Direct Energy's operations have experienced twelve straight months of net customer gains through September 2005 resulting in a net cumulative growth of 112,000 customers.

The enabler for Direct Energy to fund the unique rebate and rate stabilisation programmes that supported our overall growth is our powerfully integrated hedging programme. I am going to ask Bill Cronin who is our Chief Operations Officer and Head of our Energy Group to speak in more detail on how we manage our energy procurement programme in a manner that supports our financial commitment and provides us the flexibility to make investments in customer loyalty.

Growing customers and maintaining profitability

Bill Cronin, Chief Operations Officer

Thanks Phil. Just a few brief comments on this important topic. Gas prices which, because of the large gas fired generation fleet in Texas, drive power prices and are the key driver in the Price to Beat calculation, have driven the PtB price up by over 23% since May. Against this backdrop we have grown our customer base against our competitors. We have partially insulated our customers from the full impact of the underlying commodity price increases, all while being highly profitable while our competitors have not been - in fact some have noted losses.

How have we managed to make our customers, our shareholders and regulators simultaneously happy? We believe it is based on an active multi-discipline weekly working group that examines the following: energy fundamentals, competitor analysis, customer trends, plant capabilities, congestion issues, sales projections and financial planning.

We have fully hedged against our '05 exposure. We have already hedged over 70% of our '06 position. These positions were put in place before the run up in gas prices. The positions were taken in highly liquid gas markets, some from our plants and through bi-lateral contracts. We use gas as the primary hedge because it is more liquid and has tighter bid/offer spreads. It is also the driver of the PtB calculation and therefore makes sense to hedge with gas. We then diffuse any remaining heat rate exposure with options purchased in the over the counter market. This has allowed us to be in a very favourable position going forward.

PtB expiry

Phil Tonge

As previously mentioned the Price to Beat rate is scheduled to be discontinued in January 2007, after which all offers will be determined entirely by market forces. While there has been much speculation that this event would adversely impact incumbent margins, we firmly believe that this will not be the case and fully support the PUC's execution of the plan. Evidence of our position is compelling: Beginning this year, incumbents were given the flexibility to add other lower price plans to their service offers. Active marketing has taken place, but most emphasis has been placed on service quality. Therefore most customers still remain on the Price to Beat rates today.

From a churn mitigation standpoint, the flexibility afforded by the expiration of the Price to Beat rules should allow us to become much more segmented in our marketing approach supporting the retention of high value, high margin customers and allow us to put the right offer in front of the right customer through the right channel at the right time.

We are actively preparing for the expiration of the Price to Beat environment by implementing specific customer segmentation capabilities and by participating with the Public Utility Commission to determine what the road-map looks like in 2007 and beyond.

It does bear mentioning however that with the anticipated ongoing growth of our insurgent business, the mix of our Texas customers will become more weighted toward the lower margin segment. However we are committed to maintaining operational improvements to ensure that our operating profit is maintained in the previously stated 7-8% range.

US North

Much as I hate to leave Texas we will move on to look at some of our other US markets. Let's first take a look at our US residential markets.

This represents what remains of the customers we picked up in the course of the acquisitions of Energy America in 2001 and New Power Company in 2002. We have substantially increased profitability due to our rigorous management of these hedge books. There are promising signs that gas deregulation in Ohio is set to be taken to the next stage (possibly with the withdrawal of the incumbent utilities from retailing). And prospects in New York State appear promising. So we have great hopes that we can start to build sales and profits in this business once again.

Residential Services Group

Turning now to home services in the US. Residential Services Group which we acquired in October 2004 is our services platform in the US. The strategic rationale for this acquisition was to extend the energy and related services model. The initial focus is on Texas as I mentioned where the integration is going quite well. Future plans include expanding the platform to support our residential gas business in Ohio and the emerging dual fuel opportunity in New York.

The RSG business has two distinct segments:

- The first is focussing on installing HVAC systems in residential new construction. The company will perform 45,000 HVAC and plumbing installations this year, working predominantly with the largest new home builders in the US. This division has a competency in optimising the layout of its systems to maximise efficiency and to minimise costs.

- The other segment of RSG's business offers a range of maintenance, repair and retrofit replacement services to home owners. This business generally operates out of the same locations and under the same division management as the new construction business. This business will perform approximately 8,000 HVAC installations per year in existing homes.

RSG service divisions currently overlap with roughly one third of our customers in Texas and it is a strategic objective that we raise the profile of that footprint through tuck-in and adjacent acquisitions.

Home services and energy

This slide illustrates the three legs of our energy and services "go to market" strategy.

Starting from the top left we leverage relationships with home builders for whom RSG does HVAC installations. We do this to build a unique channel of distribution. We then

contract with the builders for Direct Energy to supply power during the construction process for model homes and for inventory homes. The builder then recommends us for ongoing service to the home owner and receives a modest commission for successful conversions. This is a powerful channel for three reasons:

- First moving is a time when consumers are rife for making energy decisions.
- Second, our integrated approach with RSG cannot be replicated by our competitors, effectively locking them out.
- And finally, these customers that we are acquiring through this channel have a significantly higher than average usage profile which combined with a low cost to acquire, translates into a higher overall customer value.

We have converted over 60% of the residential energy customers available under this programme since we began in January 2005 - again at a substantially lower cost to acquire.

Moving down to the right, we are also generating new growth by cross selling maintenance and energy contracts between our power and our HVAC service customers. We are converting 7% of our existing electricity customers and 12% of new customers to maintenance plans - again at a substantially lower cost to acquire. We have increased the size of the services contract base in Houston for example by over 20% thus far.

Finally we have also been successful selling energy to service customers, converting about 5% of RSG's service calls to electricity sales. So we are quite excited about the performance of this business thus far.

US Business Markets

Switching to business. Our Business Markets business in the US is younger than what Bob Huggard talks about in Canada, having been built organically since the middle of 2003. As of June 2005 this business served electricity in Texas alongside of the residential energy business there. And served gas in the US Mid West (Illinois and Ohio specifically) as well as the North East in Massachusetts, Rhode Island and Connecticut.

Both businesses have successfully demonstrated our ability to organically grow. Since entering these markets we have contracted volumes of over 85 million therms and 4 TWh.

The economics of both our power and gas businesses reflect their early stages, not yet generating positive operating profits. However as this business matures and we pursue growth at 40-60% per year we are targeting overall operating margins of between 2-3% for this business which would generate returns well in excess of our cost of capital and it will have low risk with our supply fully hedged upon customer contract signing.

Business Markets strategy

The US business markets represents the core of our growth opportunity in North America where we build on the growth success in Texas electricity and US North gas and electricity to date. As with our Canadian business markets, our key goal is to achieve margins and an operating structure that will ensure returns on capital employed in the mid teens. And we will capitalise as Bob mentioned on a key benefit of being part of the Centrica Group, the credit strength to drive a material insurgent wedge into these

markets while competitors shake out due to market volatility as we have already seen recently in both Texas and in the North East.

US North expansion

North East and Mid West business markets continue to have robust and expanding competition and represent a very large material market opportunity. These eligible power and gas markets are as large as Texas, Canada and the UK combined.

Earlier this year we entered the business electricity markets in the mid Atlantic area, Pennsylvania, New Jersey, Maryland and in the New England power pool. We will build upon this success to push into New York in 2006 and eventually expand our footprint to a total of 16 States within five years which will increase the size of our markets in which we operate by three times in gas and five times in power. Our forecasts are that, excluding Texas, New York will evolve into the most active and attractive market for retailers over the coming five years. This is a cost-effective adjacency-driven growth opportunity that will leverage our Canadian experience, leverage our local market knowledge, operations, regulatory relationships and EMG capabilities. We will minimise risk by hedging volumes back to back with customer contracts.

Leveraging services and technology knowledge

We are also leveraging our Canadian experience in service and technology to grow our business markets. We are building similar capabilities in Texas and we have a number of early high profile wins to demonstrate the success of this differentiation from our local competitors. This brings us important electricity relationships which raise our credibility in the market place. You see some of the examples up there: one example is the partnership that we have with the nationally known Dallas Cowboys football franchise. We provide power and services to the stadium and the practice facilities. We also have a highly visible marketing presence as a result of this agreement.

US Retail summary

So finally, over the past few minutes we have provided insight into what we feel is a strong set of accomplishments as well as a very strong set of opportunities. We have a strong position and a fast growth pace in a growing market in Texas. We have a huge opportunity in business markets that we can nimbly address by leveraging cross market experiences. And we have a services business that we can differentiate ourselves from others to improve customer and cost performance across the spectrum of our business residential and commercial.

So that is the US and I would like to introduce Mike Hogan who will speak to our upstream power and gas businesses.

6. Upstream Gas and Power Generation

Mike Hogan - Senior Vice President Upstream Gas and Power Generation

Good morning everyone. Let's begin with a broad overview of our current Upstream Businesses.

Upstream gas overview

We first acquired upstream gas assets along with the initial investment in Direct Energy in 2000 and we have consistently invested in that business to replace reserves and grow the business as market conditions permitted.

As you can see here, we have maintained an aggressive development programme. We have drilled over 1,200 new wells over the past five years or roughly one new well every 36 hours. The results of that programme have been impressive. Not only have we succeeded in stabilising our reserves position in a difficult environment, but we have consistently delivered returns in excess of 15% while creating incremental value for our downstream procurement activities. I will address the upstream gas strategy and business execution in a bit more detail momentarily.

Upstream power overview

We began building our upstream power position in earnest in late 2003 and 2004, resulting in a combination of asset ownership and long term power purchase.

Bastrop and Frontera were both acquired in 2004 at what now appears to have been the bottom of the market for power assets in Texas.

Additionally we entered into a 15 year agreement to purchase the full output of the Buffalo Gap windfarm which is scheduled to go commercial by the end of this year. AES is developing and will operate the facility. At the time the contract was signed in June of this year, it was expected to create good value for Direct Energy and the value has only grown since that time.

Again I will be addressing the upstream power strategy and business execution in more detail momentarily.

Hedging strategy

To put our upstream investments in context let me first say a few words about our hedging strategy and procurement strategy.

Procurement risk management is at the core of our business and financial philosophy. We take it seriously and we operate under the risk management policy and procedure guidelines of the Group. Our policy is to price-hedge substantially all of our weather-normalised load for forecasted sales. As Bill has said, this is an option that is generally available to us in the North American markets and it results in a fundamentally different risk profile from what you are accustomed to seeing generally in UK retail energy businesses.

Our Energy Management Group has two teams of seasoned risk management professionals operating out of Calgary and Houston with a full range of expertise in wholesale electricity with derivatives trading, load forecasting, fundamentals analysis, storage and transportation management and risk management.

In most of the markets in which we operate there is generally ample liquidity relative to our requirements. Our procurement strategy is to hedge the maximum amount of price exposure that is practical given the size, duration and scope of our supply obligations. Anticipated volumes including swing requirements are covered using our own

production, long term bi-lateral contracts, spot and forward purchases and derivatives. We trade with a large number of creditworthy counter parties including the large investment banks. Credit support is provided by Centrica guarantees or letters of credit. We lock in basis risk and ancillary service requirements as liquidity permits. Basis refers to the differences between the prices quoted at the major trading hubs and realised prices in the various market areas where we deliver commodities to end-use customers. Those differences can be large and highly volatile. All exposures are managed within prescribed limits and positions are tested on a daily basis.

Asset strategy

Our upstream asset strategy is closely tied to our hedging strategy. It is motivated by risk reduction in support of our downstream businesses. But increasingly our assets are expected to be value creating plays in their own right.

We scale our upstream ambitions based on the scope of our downstream requirements with target cover ranges driven by perceived short term and long term risks in the wholesale markets as well as by the market value of assets relative to our view of value.

In upstream gas we generally aim to cover between 20-30% of our retail requirements with production, though current market conditions make acquisitions challenging. As a result we have focused on growth through organic development which has been quite successful as we shall see.

In power, wholesale markets are somewhat less liquid and transparent, leading to hedging targets of 35% or more of our retail requirements. This has been facilitated by the fact that until very recently the limited number of merchant power asset transactions that have been done have gone off at distressed asset values.

Upstream production is sold forward to our retail businesses at market, at the time of commitment, thereby presenting a pure retail margin in the downstream books. The margin improvements available from production margins and avoided bid/ask spreads, is consolidated at the Direct Energy level.

Our asset ownership allows us to reduce counterparty credit risk, free up our own credit capacity, avoid large bid/ask spreads and give us length in our books that might not be available contractually on favourable terms.

In Texas where we have a large proportion of shaped load associated with our "full requirement" supply obligations, our plants play an extremely valuable role in providing optionality which might not otherwise be available in the market on attractive terms. As I will illustrate in a moment, both our gas assets and our power plants have been superb investments and are earning very good returns.

Acquisition of power assets

Let's look at the upstream power business in greater detail.

To date our upstream power activity has been dominated by Texas since as I mentioned our large shaped load there makes the optionality available from asset ownership highly advantageous. We have two gas fired combined cycle plants with a total capacity of just over 1,000 MW and both bought in 2004 for an average price of just about $275 per

KW. Both plants are recently commissioned, flexible and well located relative to our retail load. Our Texas generation meets about 25% of peak demand during our peak month of July. In volume terms our generation is forecast for 2005 to meet 30% of our 12.9 TWh of residential and small commercial energy requirements.

Since we bought the plants, reserve margins in ERCOT have declined due to load growth and withdrawal of capacity from the market. Plant performance has also been dramatically improved under Direct Energy management, including a significant improvement in plant availability and reliability and enhancements to increase peak hour capacity.

Although there are no recent transaction comparables, using updated power curves the plants are now generally considered to be valued at about $400 a KW or approximately $125 million more than we paid for them just about a year ago.

In addition to the value created in the plants themselves, the flexible production they deliver has allowed our Energy Management Group to tailor their electricity supply portfolio much closer to the actual profile of our retail supply obligations than what can be procured efficiently in the open market in many cases. In fact we have often been able to profit from the fact that many others in the market do not have access to the same optionality.

The UK market – a leading indicator

The significant increase in the value of our power assets is also supported by reference to market developments in the UK. We find it useful to track trends in the UK merchant plant market since for at least the last decade trends in the US merchant market have fairly reliably replicated, with a lag of one to two years, developments in the UK merchant market.

This chart is similar to that on a previous slide, but shows the picture from a UK perspective. As you can see the collapse in asset values began just about two years ahead of the US collapse. The decline in reserve margins and the recovery in spark spreads are similarly about a year or two further along than in the US. And asset values have already recovered quite strongly as would be expected from the sharp rise in the spark spread curve.

In North America we are already beginning to see a market reaction in place like ERCOT and PJM East (which is the mid-Atlantic market) to a perceived tightening of reserve margins. In reality there remains a significant capacity overhang in all but a small handful of markets such as California and South West Connecticut. But early signs of a market recovery combined with a glut of private equity money chasing these assets in this sector has meant that we have already begun to see asset values increasing sharply in certain markets. In the meantime, while the opportunity remains, we continue to look for attractively priced mid-erit and peaking plants and we may even contemplate base load plants in Texas.

Regional wholesale power markets

In the US North East we don't currently see ownership of physical assets as crucial to our market entry at this early stage. The New England power pool, the New York power pool and the mid-Atlantic power pool are generally liquid and our load there is currently

small relative to the total traded volumes. Nonetheless some assets in these markets are trading at still depressed values and we are keeping a watching brief on acquisitions that would create value and provide future risk reduction benefits.

As I stated previously, specific liquidity restraints around shaped load in Texas make asset ownership a strategic imperative there compounded by the fact that we occupy a more significant share of total capacity in that market. However even in Texas our overall trading requirements comprise less than 10% of the daily traded volume in the next day delivery market. So quite a bit of liquidity in general.

Ontario's electricity markets have recently been reopened as Bob referenced and offer good potential for growth. However the development of a robust wholesale market has yet to catch up with the retail opportunity. We are working closely with the Ontario government on increasing wholesale market activity. The measures that we have suggested including a public auction of capacity by Ontario Power Generation have recently been accepted and announced. However at this time a lack of wholesale market transparency limits our ability to address the issue through direct investments in long term assets.

Upstream gas – operational excellence

Now let's talk a little bit about our upstream gas business. We have successfully replaced reserves over the past three years with limited need for recourse to acquisitions. Our organic development programme, currently running at approximately C$100 million per year, has demonstrated strong capital programme management capability and has consistently produced after tax returns in excess of 15%. Our finding and development costs are running at roughly half of recent M&A valuations per 1,000 cubic feet of reserves.

Complementing our success in organic development we are also one of the most efficient operators in Western Canada. Compared to all Canadian oil and gas Trusts, we rank among the most cost efficient operators in the industry. We have developed particularly valuable expertise as one of the pioneers in Western Canadian coal bed methane as was referenced earlier, expertise our Centrica colleagues have recently began to leverage here in the UK.

This demonstrated excellence is critical in underpinning the value embedded in our upstream gas business. And the value in that business is substantial.

Attractive gas asset position

Our upstream gas business is in an attractive part of the Western Canadian sedimentary basin with high working interests, contiguous acreage in core areas, a very high percentage of gas in our production and an attractive reserve life index.

We have been active developers of these reserves with a good position and a proven track record in coal bed methane and in expanded development.

Our current strategy is to replace reserves organically through an aggressive development programme while being very selective in a fiercely competitive acquisition market.

Based on an extensive analysis by outside financial advisers using a broad range of comparable Western Canadian gas and oil companies, we are highly confident that the market value of our upstream gas business is in the neighbourhood of a C$1 billion or approximately double its book value.

Upstream summary

In summary, our assets are delivering real benefits in our procurement efficiency and risk management. We have realised significant value creation from our assets in their own right. Our acquisition track record is strong, but our demonstrated organic development capability reduces our reliance on acquisitions. The value of our assets is underpinned by strong operations management and the assets are delivering a solid earnings stream and valuable optionality when teamed with our retail positions.

I will now turn the podium over to David Clarke. Thank you.

7. Financial Review and Valuation

David Clarke - Chief Financial Officer

So last but hopefully not least to the financials. And bringing all of what you have heard earlier back to some hard numbers.

Recent financial results

This is intentionally a very busy slide to start with to help reinforce the diverse nature of our business and it is actually just a summary of the financial information published on North America for the last five half year reporting periods.

You will have noticed that we provide rather more limited information on our individual markets than say British Gas due to having multiple businesses in multiple geographies. There just isn't enough space to even in a limited form, as we would completely monopolise the external documents. So the aim of the following few slides is to give slightly more detail on the constituent parts to aid your understanding of the shape of the overall North American Portfolio.

However you will note first from the summary numbers above that there is some seasonality of profits. This is dampened by Texas with high consumption in the summer, due to being mainly air conditioning load, helping to offset the Canadian and US North East Gas markets which have higher consumption in the winter.

And overall the bottom line is trending upwards and operating profit as diversification has increased. But the increase in operating profit is not as fast as that in turnover. This is a result of our move into lower margin markets which going forward will be exacerbated by the impracticality of repeating the historic profit profiles for Canada East electricity and to a certain extent the Texas incumbent position.

Operating profit trace

Our most recent half year financial results demonstrated the continued sustained improvement in year over year operating profit in our residential energy and home service businesses as shown by the green bars.

- So on Canada energy, renewal margins on gas customers in a higher priced gas market led to increased profits.

- On Texas energy increased customer numbers and the avoidance of the prior year reconciliation charge helped offset the costs of growth in the insurgent business.

- On other US energy, higher operating profit was due to improved portfolio management and procurement processes.

- And on home services we benefited from the RSG acquisition completed at the end of 2004.

At the same time we do have a couple of red bars.

- Firstly we continue to invest in new markets which provide our growth in the future, primarily in the C&I space through our Business Markets groups in various geographies. The initial upfront investment to acquire customers and build the business compresses our operating profits in the short term in this business segment.

- And we cut back on our energy trading activities in 2005 to give primary focus of EMG to their procurement role.

Canada residential energy – financial trends

Moving onto some more detail behind the individual business units.

The Canada residential energy results presented externally cover our Canada East business, the Canada West regulated and deregulated businesses in Alberta and also our upstream gas business. The latter is not reported separately as in the UK at the moment because almost all of the gas production is transferred to the downstream business at market prices at the time of commitment rather than at floating market prices as in the UK, so as to match the fixed price sales to our customers. Therefore any valuation of this part of our business needs to fully reflect the fact that only uncommitted future production will move in line with market prices, whilst the existing committed production needs to reflect the internally contracted prices.

The Canada East mass markets business is in a transitional phase with gas customer numbers stabilising after a few tough years and the electricity market in Ontario having now reopened, although as we have already said, previous high profits there will not be repeatable. Short term profitability in this market will be impacted by the end of the Electricity MPMA rebates but also by the backwardated gas curve, so greater focus in the short term is being given to reducing operating costs to help protect the bottom line.

The Canada West Mass Markets business is also in a transitional phase, but a rather different one. The focus is on both administering the acquired regulated business in an optimal fashion, and this will not be a driver of profits under the current regulatory regime, whilst we grow the deregulated business organically, neither of which are easy tasks in the current environment. However in line with expectations at the time of acquisition, the regulated business is designed to broadly break even, but we are incurring short term losses in the deregulated business as we start up. Both cost to acquire and cost to serve processes must be segregated under the existing regulatory

rules, so this prevents any significant exploitation of potential scale benefits for the deregulated business.

Overall as indicated before we see customers in the deregulated business growing at around 5% per annum and delivering sustainable retail operating margins of 4-5% which excludes any upstream gas margin between the transfer price and the cost of production.

Texas residential energy – financial trends

The Texas residential energy reported results cover our acquired incumbent CPL/WTU businesses and the organic Texas Direct business being built up mainly in TXU's and Reliant's incumbent areas. Additionally the results of our two power stations are embedded here, similar to the gas assets in Canada.

The Texas business continues to be a major contributor to North American profits through careful attention to the PtB process as has been explained allowing maintenance of healthy margins in incumbent business despite the volatile times. Current margins may be squeezed over time, but we do not expect this to happen too quickly.

The insurgent business is now achieving significant scale, although its recent margins have been squeezed by the very market conditions that have worked to the benefit of the incumbent business. And the path to profitability has been constrained by short term cost to acquire as we grow the customer base and implement major process reorganisation.

Future growth in Texas will be aided by layering on the services proposition to increase customer stickiness and thereby reduce expensive churn. As per our earlier guidance, we expect this business to be able to grow at around 5% per annum in terms of customer numbers and to be able to sustain 7-8% retail operating margins for the medium term.

Other US residential energy – financial trends

Other US residential energy covers our mass market operations in the North Eastern States, currently mainly Ohio, Michigan and Pennsylvania. Although relatively small in scale, this business has seen significant rationalisation in recent years and has now moved into profitability on its mass market operations. The individual existing mass market businesses offer something of a contrast, with Ohio now showing good growth but Michigan continuing to decline - a difficult market due to the utility processes there. These existing markets are not seen currently as major engines of growth, but we now have commenced our New York entry which offers a lot of potential.

Overall we are looking to achieve average revenue growth of 10-15% per annum and sustainable operating margins of 2-3%.

Home services – financial trends

The Home Services business segment covers all of our residential home services operations, primarily the Ontario based business including the Waterheater Income Fund and the Residential Services Group acquisition in the US, plus our fledgling businesses elsewhere.

You should note that the figures on this slide for the Canadian business include only our 19.9% share of the Consumers Waterheater Income Fund accounted for on an equity basis. This differs from the publicly disclosed financial information where the accounting rules on control require us to fully consolidate 100% of the results of the fund, but provides a better understanding of our underlying ownership.

The Canadian business continues to show healthy growth in customer numbers, steady on waterheaters, but more positive on protection plans. The next challenge remains to convert this to stronger bottom line profits. The business as you have heard is emerging from a transformation programme, leveraged off learnings from the UK, which has depressed our short term profits. However it now has the necessary infrastructure for adding scale at minimal incremental cost.

The acquired US business is delivering in line with our expectation and, as you have heard from Phil, we are actively implementing the cross sell opportunities in markets where there is overlap between the service and energy business as we look to replicate our Canadian model.

As indicated earlier, in Canada Home Services, we are expecting top line growth of 7-8% going forward and operating margins to grow to as much as 14-16% whilst the US should achieve 5% per annum revenue growth with margins increasing to a sustainable run rate of 10%.

Business markets – financial trends

And finally this business segment has achieved huge growth in 2005 on the top line and represents a major growth engine in the coming years. It offers excellent opportunity but we will see lower percentage margins than the residential markets but with a satisfactory return on capital.

Much of the business is currently in start-up mode with the Canada East Energy and Services businesses being the slight exception, although it too is in a huge growth phase. Short term profits in the start-up markets are being constrained by the normal growth-related expenditure including cost to acquire, but also by tight margins in all markets which are proving to be very competitive, plus the impact of the current backwardation in the gas curve which compresses our margins in the short term on multi-year products.

As you have heard, entry has commenced into various C&I markets in the North East US as the vehicle for future growth and they are leveraging off the existing residential mass market structure as much as possible to minimise the investment before reaching ongoing profitability. We have found this a viable strategy to offset the lower margins available in the C&I segment.

The earlier guidance on this market was that growth in Canada is expected to be in the order of 15-20% per annum with margins growing to the top end of the industry range of 3-4% plus higher growth of 40-60% per annum in the US at slightly tighter margins.

Return on invested capital

Just to finish the history, looking briefly at the return on invested capital achieved to date in North America, here we have defined it as NOPAT before depreciation divided by

average gross invested capital for the year. And we have presented the numbers both in terms of the underlying statutory tax rate for North America of 38% and the effective tax rate incurred allowing for brought-forward losses, the latter of course yielding rather more fluctuating results.

As you can see we took a bit of a dip in the statutory tax rate based figure in 2004 as we invested more capital in acquisitions, the two power stations for example. But the 2005 estimates see us as achieving a positive spread on the group WACC and we expect to move into double-digit returns in the medium term.

Turnover mix

So having had your history lesson, what of the future? We have provided some guidance on each of the businesses, so now to the overall picture.

In terms of top line growth we have said we see opportunity for selective entry into new residential markets, whilst our existing residential markets produce moderate growth. In contrast we foresee much greater expansion in our C&I businesses, through our Business Market operations in Canada and the US. The end result will be a much more balanced portfolio both from a geographic and customer segment perspective as shown by this pie chart on turnover.

Operating profit mix

Similar to turnover the growth in our C&I businesses will result in a larger proportion of our operating profit being earned by this customer segment, although this is still only around 13% by 2008. We also expect to expand our service offering over this time frame. When you get to 2008, whilst residential energy will continue to be the majority of our forecast operating profit, we expect it to be much closer to half by then than the current two thirds and with a significantly reduced reliance on Texas.

Valuation benchmarks

In the competitive landscape section, Maura noted there is no one perfect comparator for our business. We therefore thought it would be helpful to provide some of the publicly available information around valuation benchmarks which might be appropriate to consider in the context of valuing Direct Energy.

I am not going to comment in detail on these various benchmarks, but you may like to review them after the meeting in the context of the business information we have provided. I think if you do this it will demonstrate a sum of the parts of opportunity that is significantly in excess of current analysts' consensus.

But just to provide some context on our choices:

- The Energy Savings Income Fund is our largest competitor in the Canada residential markets.
- In Texas our main competitors are TXU and Reliant although we have to recognise that both are part of integrated companies with upstream generation. So we have also included the acquisition metrics for GEXA Corp which was a small commercial retail business in Texas and the North East acquired by Florida Power & Light earlier this year.

- For the C&I business, there are two good comparables embedded in larger companies: Constellation New Energy and Strategic Energy which is part of Great Plains.
- There are no recent comparable transactions for our CCGT plants in Texas. So for upstream power we have reflected our own estimate that Mike mentioned of what Bastrop and Frontera would be worth if we were to simply revalue the plants on today's forward power curves.
- And for our upstream gas assets in Canada the quoted value on the chart is the mid-point of the range of recent sale transactions in North America.

Financial summary

So to summarise I hope you will agree that we have an impressive track record on the financial front. There is absolutely no reason to believe that this cannot be continued into the future. Our North American operations currently represent a good portfolio of businesses which help dilute our exposure to external factors or individual markets. And this will become even more balanced between the various business sectors and geographies over time. We are already making a spread on the group WACC at effective tax rates and expect to move to double-digit returns in the not too distant future.

Importantly, based on our current forecast, we will generate sufficient cash to self-finance the growth in our business covering increased working capital and our maintenance capex expenditure of around C$150-200 million per year plus some additional power station capacity in Texas without any further capital injection from the UK over the next three years combined.

8. Summary

Deryk King

Thanks David. That was a lot of information during the course of the morning. So you will be relieved to know this is the final slide of the day. I started my career in sales and marketing so you would expect me to finish with a bit of a push on our proposition. So let me finish by summarising by what we see as the investment case for North America.

First of all we will be a material contributor to Centrica's future growth by selecting carefully and prudently from the huge raft of opportunities in North America.

We already have a footprint that is sufficiently diverse to mitigate specific market related risks but is nevertheless focused and tightly managed.

We believe that our core residential and services positions have critical mass and leadership positions on which we can and will build.

And the huge business markets opportunity can be exploited with relatively low risk and within our local resource capability.

We have industry-leading energy management skills and growing upstream capabilities that offer both reduced risk and enhanced profit contributions in themselves.

And our forward development plan - our "sustain and grow" strategy - again is relatively low risk and as David has said, can be funded into the medium term from our own North American cash flows.

I think my team has consistently demonstrated its ability to spend capital wisely, creating value and building a profitable and scale business. And the fact that others have tried and failed is a testament to our management and bench strength both within this room and back in North America.

And finally let's not forget execution: seizing opportunities to improve current operational performance as well as delivering growth. We never forget that.

So the result is double digit revenue growth going forward, what we hope and believe will be robust operating margins and progressive improvements in our return on capital into double digits over the next five years.

As I said, I am a marketer, not a mathematician but by my calculation if we could grow our top line at say 10% per annum, and if we can sustain operating margins at today's 5% then in three years time we are looking at a business with revenues of around C$10 billion, EBITDA well in excess of C$700 million and EBIT somewhere north of C$500 million.

So taking into account our performance to date, the forward growth potential of the business and the comparator benchmark valuations that David shared with you, it won't surprise you to hear me repeat that we believe that Centrica's North American business is significantly undervalued by the market. And I hope we have given you enough information to make you believe that today.

9. QUESTIONS AND ANSWERS

Question 1 Ed Reid, Cazenove

Just one question really. I think Phil and Mark Clare have talked about British Gas aiming for two things which is an advantaged cost to serve and an advantaged cost of procurement. And I just wondered on the Canadian Retail business how you look at those two areas?

Deryk King

We are one of the largest procurers of energy in Canada, both gas and electricity, and Bill Cronin's team in Calgary is a major player in trading and wholesale markets across the whole country. And as our Business Markets operation expands that will grow our volumes quite dramatically. S o we are and aim to be a major player. We believe we have a good handle on the market place but we are acutely aware of the trade flows. We manage some very significant gas storage and transportation positions at key hubs in Canada, particularly at the Ontario border. And we believe that that gives us a competitive and, one hopes, through time, an advantaged cost of goods.

Bob Huggard

I would say we have two key initiatives under way right now. One is to put as much money as we can into the front line ie. we need to focus our investment in people to those that are going to be revenue producers like our sales engineers, like the front line. As well we are moving as much fixed costs into variable costs. So we had had a model where we owned a lot of our sales force. We are moving some of that sales force and taking more and more of that into partnership relationships so that we can flex as the markets change. Our cost to serve, a lot of it is covered through arrangements with the utilities or their affiliates on billing so we have very little in the way of bad debt to have to move and they take a lot of the risk. And we ride on that utility bill which gives us some cross branding and coverage. So our emphasis over the next three years in managing our costs are going to be to put more money into our front line people to build that, particularly engineering staff and to grow more variable than fixed.

Mike Hogan

I was going to make the same point Phil and I were just talking about. Deryk referenced our cost of goods and it is worth pointing out as we'll talk about later, that the wholesale markets, particularly in gas, in North America are much deeper, much broader and much more fragmented than they are here in the UK, which does give us, particularly with our purchasing scale a much stronger ability to control our cost of goods by accessing a very competitive wholesale traded market.

Bill Cronin

I just wanted to give you one quick example, because you were talking about the procurement side. Let's take Canada for instance where we are procuring more than a BCF a day for our load. Now most of the production zones are out west in Alberta where we have upstream gas. So even right there we have some advantage in the fact that, as prices rise, the value of our upstream gas portfolio also increases because gas is a driver also of the economics of our plants. The plant values have also gone up significantly. On a day to day basis for instance one of our key costs to our customers is the TCPL toll and that is $1.16 and that is built into the rate of our customers. But because of our procurement strategies we are able to come in quite a bit less than $1.16, we come in at about $1.08. Now 8 cents is actually quite a bit on the volume that we are moving at 1 BCF a day. So there is a procurement advantage that others don't have because of the size of our business. Also the weather side. Obviously as a full requirement supplier there is weather risk, the daily swings, and because of the geographic diversity - obviously Texas has summer type risks where the volumes are hard, Canada East would have you know the Ontario market would have weather risk in the winter. So by the time you get done with the geographic diversity, we can actually lower our weather cost versus competitors that have smaller market share or are geographically less diverse.

Question 2
Bobby Chada, Morgan Stanley

Two questions. You have got some quite sizeable revenue growth targets and lots of them are related to growing business or commercial and industrial customers. What will that mean for working capital requirements? And secondly, just to follow up on some of the procurement issues you talked about. I think I am right in saying at one point you had some long term contracts to buy power in Ontario. Are these still in place and how long do they run for if that market is opening up and is a source of growth?

Deryk King
I'm going to answer the first question very quickly as David will touch on this later. As you saw our C&I growth targets are very ambitious in revenue terms. The operating margins are relatively low. You have 2,3,4% typically. If there were large working capital requirements you can see that would be a difficult business to make a return on. The fact is that the net working capital requirements for our C&I business are quite manageable and those operating margins turn into a very respectable post tax return on capital which is how we measure the success of those growth plans. And I won't steal David's thunder because he'll talk about the numbers in his part of the presentation.

Bill Cronin

First of all on a working capital side, a great deal of that growth is in power and power does not have inventory and therefore has less of a working capital component so it is not as significant as you might first expect because of the high volumes.

And then in terms of the long term contract that you questioned, you are correct, it was Bruce Power. That was the major contract that supported our long term energy electricity position. That runs out. It is perfectly matched with our actual demand side. The contracts that we sold years ago, these were five year contracts that are coming due in early part of '07 and therefore we are fully hedged on that and we are talking to Bruce right now about re-upping. But we are not ready to renew our contracts with our customers yet. When we do we will look to match that off again with Bruce and other suppliers and we have been selling actually quite a bit lately through Bob's business and we have been able to procure load through the bilateral markets which includes Bruce, Constellation and others.

Question 3
Andrew Mead, Goldman Sachs

Can I just check. On your revenue growth going forward, can I just check that is all primarily driven by volume growth rather than the assumption about price increases going forwards?

Deryk King

Yes. It is a risky thing in today's environment to give any revenue growth projections and that is why we are being vague in terms of low double digit. But that low double digit takes into account some movements in the energy curves but not up. We are forecasting I think someone referred to backwardated curves. We are looking at quite significant backwardation in both gas and electricity curves going forward. So we would expect the energy deflator to be at least as big, probably larger than CPI. So the short answer to the question is yes, it is volume growth and not pricing.

Question 4
Andrew Wright, UBS

Rather over simplifying but the picture in Canada appears to be one of say limited opportunities in the residential side which has been compensated for by accelerating the

growth in the services side and also the C&I. Does that potentially expose you to greater competitive pressures because presumably the barriers to entry in the commercial and industrial side are potentially less than in the residential side where you don't need to have the mass marketing and mass servicing capability?

Deryk King

I can see how you would draw the conclusion that it is all about C&I but if you go back into the material and look at what we have said you will find that although we are slightly downbeat on residential energy we still see it growing significantly in Canada. We see growth in Alberta being slow but positive. We see growth in Ontario, once again building on electricity to start selling dual fuel products. And we see ourselves growing our Manitoba gas business and that is all in the residential space. In the C&I space the barriers to entry are quite high. The combination of skills both procurement, hedging, retail skills to make a success of what is a very low margin C&I business are extraordinarily complex. And on top of that you have the credit requirements required to sell multi million dollar contracts. And the credit risk associated with very large energy users who are your customers. So we are actually finding the opposite in this currently high priced and volatile market. We are seeing competitors come under severe credit pressure, some of them thinking about or even withdrawing from the market place. And as I think, I can't remember whether it was Bob who said this or myself, it is the large well capitalised skilful players who are going to make a success of that business. So we're OK.

Question 5
Martin Brough – Dresdner

Could I ask a couple more questions about the Ontario electricity situation around two issues. One in terms of the loss of the mitigation proceeds. How much do you expect those to be in 2005 roughly? So how much is disappearing from that? And the second part was when the contracts come to an end in '07 what actually happens? Are customers forced to make decisions on how to renew? If they just do nothing and there's inertia, what happens to those customers?

Bob Huggard

Well on the contract renewal side, obviously we are very aware that we have a large number coming due. We have started to begin a process now of starting to segment and identify those clients that we'll be going after. They do need to make a positive renewal declaration, otherwise they will flip back into the system supplier. So we are developing both our products so whether they be declining, fixed or floating cap, in conjunction with our dual fuel capability of gas, to provide them with some options on their renewal period. But if they choose not to renew then they would go back into the system supplier. We are forecasting over 85% renewal. We are seeing 93% these days in our renewal activities.

David Clarke

On the MPMA, it actually ends in April 2006. There has been an early termination on the business markets and it would have hit us around the C$10 million mark, but we are actually recovering that from the customers. It was a loss of what was called the

provincial benefit. But we lose the full MPMA in April 2006. It will be in the order of C$35 million in that year.

Deryk King

The financial forecasts or expectations that David will talk about later will fully embrace any penalty from MPMA and anything else that's happening in the market place so we are looking at our numbers net of all those costs and events.

Question 6
Nigel Hawkins, Libertas Capital

I was just looking at the Canadian Home Services section and I notice you have got some quite aggressive overall margin projections. On page 39 I do note that since mid 2003 on home services overall we have seen a doubling of turnover yet operating profit has remained broadly stable. So I was wondering on your page 17 of your presentation where operating profit is £8 million on turnover of £132 million which I think give a margin of about 6%, how you could you justify going to a forecast of operating margins of 14-16%? Perhaps it's over a long term period?

Deryk King

I think as Bob pointed out the operating margin expectation of 14-16% might look aggressive but it is comprised of two components: about a 10% expectation on the protection plan business and a higher margin on the equity share of the Income Fund. So if I could rephrase the question, it is why do you expect to get up to 10% operating margins in your protection plan home services business? Well we said we would be honest about what we have done. We inherited a business from Enbridge which was OK but did not have particularly enhanced capability to grow. We have grown that customer base from 300,000 to 500,000 customers broadly and it has put an immense strain on the system. So we have put in place over the past 2 years a transformation programme based to a certain extent on what British Gas have done in this country. That has been quite a costly programme, but it has now positioned us to improve our performance metrics, handle the increased scale at low incremental cost and we are very confident about our ability to hit at least 10% operating margins on the protection plan part of the business going forward. And then allied with the higher margins on the Income Fund side, that grosses up to about 14-16% on the overall turnover.

Nigel Hawkins

Have you got a time period for what I think is a trebling of margin?

Bob Huggard

I came over with the Enbridge acquisition and I know at that time Enbridge needed to sell the Services group because it was not investing in it. So what we have done through Centrica and British Gas's leadership, is invest in the business over the past three years to give it the capability to grow. Over the past three months as I have come into this position, I have gone back into the numbers in detail with my team and there is a plan and there is low hanging fruit that gives me the confidence that I can sign my bonus up

to Deryk to deliver those. And we will deliver those numbers. We will hit 10% EBIT by the end of 2007.

Deryk King

Having sucked British Gas Services dry of all the knowledge they have, we have just appointed a new manager for that business called Lee Rose. Lee used to run General Electric's servicing business and more recently Sear's servicing business for the whole of North America. So we think we have got a heavy hitter now that is going to deliver on those improvement programmes. So we are very confident about that business.

Question 7
David Long, UBS Global Asset Management

You talked about the credit problems that some of your competitors are facing that you can overcome because of the parent company balance sheet. Can you quantify the amount of credit that sits behind this business and do you include that in your return on capital employed?

Deryk King

Yes is the answer to the second point. On the first point, it is difficult. We are currently sitting on some quite large amounts of cash on margin, working in our favour.

David Clarke

We have been sitting on C$550 million of cash in the bank on credit calls the other way. But we have got credit lines in place for our worst period which will be next February/March as you would expect for the winter. Those LCs go up to C$500 million.

Phil Bentley

If you are thinking about the cost of the LCs in the capital base, the answer is no. I mean it is in the charge, the LCs, as a revenue cost. We are not ascribing if you like capital in a way a bank would, if that was the point behind the question. We charge Direct Energy for any parent company guarantees that are given by the Group. The going rate for that and that is in the overhead charge I am afraid. But no we don't include a deemed capital for the LC itself. It's an OPEX. It's a big number at the moment. It is going to be running in gross terms well over a couple of billion dollars for each power and gas.

Deryk King

But just to make sure it was clear. When David talks about return on capital later, it includes the working capital that we deploy. And as Phil said, we pay full commercial rates for any credit support the Group gives us. We get nothing for free from the Group.

Question 8
James Hutton-Mills, UBS O'Connor

Just a couple of quick questions. If you look at the Texas residential energy business and the US residential energy business on pages 24 and 29, SG&A as a percentage of sales looks to be about 14% at Texas versus 9%, ie. 500 basis points difference. I just wondered what that reflects and also on the same point you highlight that margins might come down a little bit in Texas. Is that more a reflection of commodity prices or is that more direct marketing?
And then secondly in terms of strategy for your upstream gas business and how that links in with customers. Both looking at the UK and US it seems as if you are perhaps a little bit more aggressive at picking up upstream gas assets in the US. I just wondered if you could talk about that in a little bit more detail and explain that please?

Phil Tonge

You talk about the margins in the Texas residential business. One of the things I emphasised is that we do have a continued growth objective in our insurgent business. The margin characteristics on our insurgent customers are not the same as the margin characteristics on our incumbent business. So as a mixture we are going to have a bit of margin depression on the overall base because of the mix of customers. So we expect that to continue. On the flip side, as I emphasised we are doing what I would consider pretty heroic efforts to continue to drive costs out of the business by reducing our costs to acquire and costs to serve to offset some of that margin pressure.

David Clarke

On the SG&A point there are two factors at play: one is in Texas we are incurring a lot of costs to acquire in the insurgent business. But the more fundamental difference is that in the north they are utility-billed whereas in Texas we bill them ourselves. So our cost to serve there includes all the billing costs where it wouldn't up in the north. There it is done through the utility, they bear the bad debt etc.

Mike Hogan

I will just take the upstream gas question. A couple of differences: one, the production profile on typical Western Canadian sedimentary assets or reserves is very high production in the first two or three years and then very rapid decline which presents its own challenges, if you are relying entirely on acquisitions to keep production steady, but it does mean that we and others are prepared to pay more aggressively on the front end of the forward gas curve. Whereas much of the production that we look at acquiring in the UK - North Sea etc- the production profile is a little bit more back-ended with a slightly less aggressive forward curve at the back end of the curve. So you will see some difference in valuation strictly because of the production profiles, compared to relative production profiles between the two different types of reserves. And I think it is also fair to say that over the past few years there has probably been a bit more deal flow in Western Canadian assets than there has been in North Sea assets.

Question 9
Andrew Wright, UBS

You presented your Canadian and Texas residential numbers including the contribution from the upstream assets embedded within that. And you pointed out that the price that they effectively receive in those upstream assets is impacted by the contracting

arrangements effectively at a lag because of the longer term contracts you have with your customers, three or five years. Could you go through how those numbers will change if we have a sustained higher energy price environment? So for example the type of spreads we are seeing in Texas now and the high gas prices we are seeing are sustained. Will that lead to overall higher profitability across the value chain which reflects the enhanced stand alone value of those upstream assets or will you expect to absorb that and will it lead to effectively more competitive prices to customers?

Deryk King

It is quite complicated to explain. I hope we have done so, but I am going to repeat what colleagues have said to make it absolutely clear. Let me take Ontario gas as an example. We go out and sign some customers on five year contracts so we have a commitment. As we develop our upstream assets in Alberta we will create a five year strip, through exploration, through production, through development. And we sell that five year strip into the retail book at the market price of the forward curve on the day. So on the day that transfer takes place the retail book is buying at market - the five year strip. And the upstream book is selling at market. If then gas prices rise as they have recently, the upstream book captures all of the incremental - as prices go up and we develop more gas which is not hedged in the downstream book, the value of that gas rises. If we then subsequently transfer it into the downstream book then it is at a higher price and the downstream book has to deal with that. So the downstream margins we suggested to you are based on fairly robust assumptions whether the gas is high or low priced, because the upstream transfer takes place at the value of the curve. But the value of the gas business in a high priced environment is significantly higher than in a low priced environment.

Andrew Wright

A related question. When you talk about that C$1 billion estimate of the value of Alberta upstream assets, does that take into account the fact that a lot of the gas is being sold at the same prices as a few years ago as opposed to prices today?

David Clarke

I will deal with the gas and come back to the power. We only commit the production from the upstream as it is being drilled, therefore we don't commit too far forward. So if you wanted to value the upstream gas business all at market it would be a little bit higher than that C$1 billion. The market value of what we have committed to the downstream book today, if you marked it to market is in the order of say C$80-90 million. So we aren't forward committing too far with the upstream gas production because these are small wells. You have heard the number of wells we drill. They are not big wells that are going to produce huge volumes, they are lots of little wells. o we commit it at that time. Yes there will be higher profits going forward and part of the offset of the C$35 million hit I have mentioned earlier on MPMA will actually come from production which is now certain enough for us to commit it, but it is committed at a much higher price than when we purchased those assets or when we drilled it. So you will see an up-tip next year in the part of the profit in the chain which is attributable to upstream gas because their marginal cost of production hasn't changed much, but the price that they are now fixing it with the downstream business has gone up. So we will see an up-tip next year that will offset that C$35 million. So Canadian residential, if we

were to publish in the same way next year, will not have the dip I forecast earlier, simply from the upstream gas production.

Andrew Wright

And similarly how will the improved profitability potentially of the power stations in Texas manifest themselves?

David Clarke

Power stations are different. They are on tolling contracts. And effectively they are slaves to EMG as part of its procurement and of course the cost of gas has moved that they are generating on. The optionality value of the power stations has gone up because obviously we are in a much more volatile market and higher price market. They will not achieve the same sort of kicker in margin because we haven't already bought the gas that they are going to generate.

Andrew Wright

And the tolling contracts, what are they based on?

David Clarke

Cost recovery. It is against the forward cost, partly the original acquisition cost, but any change in maintenance as well. So they are meant to come out broadly flat over the life. They are just covering their costs and the cost of capital that was originally embedded in the acquisition, but they don't get huge profits through the fluctuations in the electricity market because the gas isn't fixed.

Andrew Wright

So the extent to which you get competitive advantage through having those power stations will be reflected in your downstream margins?

David Clarke

That is all around the shaping. That is their value. They are mid-merit peaking plants which help us to cover off the ups and downs. They aren't base load plants that run all the time.

Bill Cronin

The plants themselves as Mike highlighted have significantly more value than we purchased them for. We sell out as the downstream load creates the obligation on the short side. We sell out that plant capacity to that load requirement. But as you look at the value stream going forward there is definitely an "in the moneyness"of those positions because the value of the plants are now greater than the acquisition cost built into it. So as we move out into let's say '07, '08. '09, this business will be the recipient of that "in the moneyness". So if you look out into let's say '07 right now, in excess of the acquisition case which has to carry the cost of capital for the firm, it is already in excess of $25 million greater than the acquisition cost. We will still transfer that at

market in ’07 to the downstream businesses. But the Group, Direct Energy will be the recipient of the excess, the $25 million. So that will fall to the upstream business.

Question 10
Iain Turner, Deutsche Bank

You talk quite a bit about expansion into the US business markets in the north. Obviously there are lots of people already in those markets, some of them large, some small, some desperate. Can you run through what you think your edge is in competing in that market compared with those incumbents?

Deryk King

I think first of all I would slightly take issue with the view that there are lots of competitors. There are quite a restricted number of competitors. Of course you have got the incumbent utilities still competing - we use the word competing in that space but that is a misnomer - they are present in that space. And the switching, the high levels of switching we are seeing reflect dissatisfaction with the plain vanilla opportunities that the utilities are offering. And then you have got the likes of Constellation, Reliant, Strategic Energy. Really you can count the number of committed retail players on the fingers of one hand. And some of those such as Reliant we know are in financial difficulty and of course North East Utilities has just announced it plans to sell its retail arm Select Energy. So this is a tough game for large well capitalised players. But our edge has a number of aspects to it: First of all our ability to procure energy in real time while we are having customer negotiations and that sounds a little bit trivial but it is actually a very challenging thing to do to link your energy management group with your sales team in shaping products that customers really want. Secondly we have talked about the services offering that we have developed in Canada and which we can transfer and will translate into our US markets. And thirdly we already have a significant residential presence out of Stamford Connecticut in the US North East and we are able to build incrementally in resource terms, keeping our cost to serve very economic.
And it is no one thing. It is that combination of factors together with terrific execution that gives us that competitive edge.
And at the margins we are talking about you need to in addition be very careful about your hedging, make sure that your contracts are backed as near 100% as you can with procurement hedges and secondly pay persistent attention to your return on capital. And as I said 2-3% operating margins doesn’t sound much. But if you talk about returns in mid teens it sounds a heck of a lot better.

Maura Clark

The other thing we might add to that is that even though there are a handful of well capitalised players, no one has a dominant market position. The market leader only has in aggregate only 20% of the market so there is really plenty of room for people to compete in that space.

Question 11
Martin Brough, Dresdner

Sorry I just wanted to follow up on the upstream gas in terms of the approximate market value of the contract effectively to sell into the downstream business. You say it is C$80-90 million and I was just trying to reconcile that with what has happened to market prices because let's say you have got two years on average outstanding on that, that's C$40 million per year in the money for that downstream sales. And you have got what, about 0.7 million deregulated customers in Ontario on the gas side. So it implies only about C$60 per customer per year in the money for that downstream hedge. And you are selling about a 1,000 therms a year to those customers. So it seems to be only about three pence per therm on those very ballpark assumptions in the money in terms of the procurement costs in the downstream under those contracts versus market prices. Which seems incredibly low given what has happened to market prices of gas?

David Clarke

It is all a timing issue because if you think that they are committing forwards and where the curve has gone we were selling from the upstream to the downstream business at around C$4.50 and it is now up at C$8-9. That C$4.50 will flow through the book. And once that is gone you will see the upstream side of it pick up.

Mike Hogan

First of all David talked about how far out production is sold and if you look at the next five years of our expected production from our upstream gas business, if you look at the percentage of that, if we are comfortable enough today to be able to predict the exact timing of that production. As David mentioned, these are all very small wells. And we are highly confident on a given well for instance if it is in the 2007 development programme it is going to be drilled at some point during the year, but depending on whether it could be in March, could be in September. So that far out for those types of volumes we are not comfortable committing them firm to the retail books. In addition all of our let's say proven plus probable production, looking forward six months to twelve months, given our internal risk guidelines we only commit 85% of that firm. 15% of it is left floating. So that also contributes both to the amount for which the upstream gas business benefits from the increase in prices, but also the smaller amount of the absolute number of the value of the hedge that is in the money or out of the money depending on what perspective you have on it. So we are only committed on production. It is a declining curve as a percentage of our forecasted production, but it is only out about effectively about a year. And that is again a function of the nature of the development programme, the level of confidence you have in predicting exactly when production is going to come on line, towards the back end of 2006 into 2007. So that all contributes to the absolute amount that we have committed to the retail business in the form of previous sales.

Martin Brough, Dresdner

If you got some gas customers say three years ago at fixed prices then you must have some incredibly valuable gas purchase contracts somewhere to be able to sell to those customers today at a profit. Clearly if you are buying in the market today, you will be making massive losses?

Mike Hogan

We only cover today about 17% of our retail sales from our production.

Deryk King

That is the number that is public previously, but we haven't mentioned today, that about 17% of our retail gas sales in Canada in the North are covered by our upstream assets, that is all. And those are, if all our customers walked away today, we would have a massive "in the money" position on both power and gas, but we hope they won't do that.

Question 12
Bobby Chada, Morgan Stanley

To go back to the business customer and the business markets and margins and returns you talked about. Earlier in the presentation you said it was easier to hedge for those customers in the US than in the UK because markets are much deeper and more liquid and you talked about hedging minute by minute as you sign the contracts with the customers. Are you able to do that for more than one year or are these business customers kind of one year contracts that are constantly coming up for renewal?

Deryk King

It is a variety of contracts from one year to broadly three years and we can hedge comfortably on gas forward for up to five years if we have to. The point is that we as a proportion of the total US gas market are tiny. I have got the number 1% in my mind, but I am not sure if that is accurate. So when we buy, even if we buy significantly from our perspective, we never move the market.

Bobby Chada, Morgan Stanley

And the power markets are liquid enough to do something similar?

Deryk King
In most of the jurisdictions in which we operate. In fact if the power markets are not liquid, then we cannot operate, so there is a sort of self fulfilling definition there.

Question 13
Nigel Hawkins, Libertas Capital

I hear you have no need for further financing for three years in the States, but I also note that in a November 2002 presentation you confirm that Centrica's international strategy was and I quote here 'to achieve a target at least 15 million customers outside the UK over five years'. Now we are over three years into that five year plan and I wonder how you are going to get to your 15 million customers?

Deryk King

Well I was hoping someone would ask me that question! I think you have seen in terms of the diversity and the scale and the composition of our business that simple customer metrics aren't any indicator of value and so I have no idea whether those targets will be met. For North America it is not a relevant question. We have given some quite clear

expectations that we are working to in North America and you can calculate back to customer numbers if you like, but I think I am more interested in the value proposition and the diversity of the business. But of course we could do silly things like convert our business markets operation into residential customer equivalents which some of our competitors do and I am sure we would get a gigantic number. But it does not give you a sense of the shape or the robustness of the business. So from the North America perspective, customers are important, but customer numbers is simply one of many metrics we use. On the wider Group situation, well we have European ambitions that might help.

Phil Bentley

Back to the famous 10 million customers that were set as a target before we even got into the market in the US. I think we sort of killed that one a long time ago so I am afraid you are a little bit out of date on that one. It was 5 million in Europe and 10 million in the US before we had even got into the markets, premised on a pace of opening of the markets that simply did not happen and therefore we needed to adjust those and that is what we did. And as Deryk says, we are not looking, and customer numbers are not a good way of measuring value creation. And if nothing else today I hope you take away, there is a lot of activity going here, a lot of value creation and actual customer numbers, we never even mentioned a number, because it is not the way we run the business today and I hope you have got that message today.

ENDS