British Gas, Calortex • Roger Milne asks him how he did it.

Peter Franklin has just emerged from four years at the coal face of domestic energy competition. A couple of months ago he severed his links with Calortex, the mains gas supplier that seemed to come from nowhere in 1995 as the world waited for domestic gas competition in south west England.

The first trial of competition kicked in at the end of April 1996. Calortex, then a joint venture between bottled gas giant Calor and oil and gas major Texaco (subsequently joined by Dutch utility Nuon), was for a long time the most successful rival to British Gas.

When the company was sold outright to National Power last month, it had 500,000 gas customers; for the last 18 months Franklin, as director of corporate affairs and development, was working towards adding electricity.

Franklin believes the electricity market is surrounded by more uncertainties than gas. Databases are not as well structured, he says, but the problems are not insuperable. He points to the success of British Gas in carving out a significant presence in electricity.

For a company as big as Calortex there were plenty of prospective partners. Clearly, had Calortex continued to expand rather than offload, it would be in dual fuel by now.

I remind him that for a long time Calortex eschewed a move into electricity. He agrees but points out that the world has changed.

When Calortex started, says Franklin, the whole public, regulatory and government consciousness was geared to the opening of the gas market.

'The proposition was to say we're a credible gas supplier and you can save pots of money by switching from the incumbent to us. In the south west when the domestic gas market opened, Calortex got 50 per cent of all the switchers.'

He adds: 'I've spent my life learning how to manage uncertainty; you have to recognise that paradigms shift and these occur more frequently and rapidly as markets change along with technology.'

Why did Calortex start so well? 'You can't explain it simply in terms of its price positioning. It was priced as the cheapest in the south west but then made a conscious decision not to be the cheapest as competition rolled out. However, it still won one in four of the switchers,' says Franklin.

He tells a nice story about expectations in the early days. As joint general manager of the fledgling mains gas supplier, he recalls sitting down with a blank piece of paper in the summer of 1995 (before the market rolled out), considering what figure to put in the business plan for the 1996 Calortex customer base.

The bottom end was 2,000 (anything less and they would have shut up shop). They guessed at around 5,000. The then Calortex managing director Geoffery Robinson suggested 15,000. 'But at the end of year one we had 43,000.'

Because of the uncertainty about how things would pan out, Franklin and his fellow managers created a 'virtual' organisation.

'The customer base could have been 2,000 or 250,000. What sort of organisation could handle that bandwidth of uncertainty?' he says. 'The solution was a virtual organisation. Whatever size we plan for is going to be wrong. Either too small so it won't be able to cope with growth or too big and the cost base will be too high to support the level of business.'

So Calortex signed contracts with other companies to manage the billing, do the selling and provide the call centres.

Franklin says that in order to compete with the likes of BT and British Gas, which have customer bases of 20 million, smaller Recs have to link up to gain economies of scale. That way they can get a good deal and still provide margins for the suppliers.

So enter United Utilities' Vertex, Northern's Aurora, Hyder Services and, from outside the energy industries, Ventura.

Franklin says: 'The presence of these service companies meant… there was little difference between handling a single fuel customer and a dual fuel customer, so effectively a single fuel supplier had double the costs of a dual fuel provider. It also created a platform for new entrants to come in because you no longer have to build your in-house administration.'

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Then the Recs, which had all toyed with domestic gas businesses, restructured.

'When they started, they set up little offices at the side or down the road, added a few people and PCs and formed a gas company. The south west and south east trial areas were characterised by that type of operation.

'The Recs have now reorganised to integrate their gas and electricity operations and call them supply businesses. They are separating out, or at least beginning to separate out, distribution company assets ahead of the formal regulatory split,' he says.

Conventional wisdom suggests margins in supply are so small and the competition so fierce that only companies with big pockets can survive. Franklin is not convinced.

'Margins are tight,' he agrees. 'There are times when the margins are wafer thin or non-existent and times when they are very rich. It's a roller-coaster. The mistake is to say what exists today is what will exist in the future. When we launched Calortex, gross margins were over 8p a therm, went down to 1p and came back to 6p.

'The market self-corrects. If margins get too thin you get consolidation and a number of players exit until you reach an equilibrium where there is enough margin for those players left.'

How many players in the domestic energy market in the future? Conventional wisdom talks of half a dozen, with some niche players.

'Logic says yes,' says Franklin, 'because you need big customer bases to drive costs down. However, if you look at the industrial and commercial market, everybody has been saying for years that there must be consolidation and it hasn't really happened. These managed services operations allow you to overcome the disadvantages of small scale.'

Franklin believes the big catalyst for change will be the split between electricity supply and businesses. 'Then people will make strategic decisions: yes I am a distribution company, I like running wires, perhaps I'll merge with someone so we can share engineers. We like running a regulated business so we'll get rid of our supply business.'

He foresees changes in ownership: US companies will want to leave, others will want to come in, including European players. 'The next two years should be a bonanza for merchant banks,' he reflects.

Franklin trained as a metallurgist and materials scientist, and went to business school before joining Shell and becoming 'an itinerant executive gypsy' working in London, Bristol, Milan, Den Hague and Newcastle.

He left Shell in 1993 and helped set up the marketing and sales co-ordination operation of leading independent gas supplier Agas at the time the Industrial and Commercial (I&C) market was opening up. He joined Calor in 1995 to head up its embryonic mains gas business, with the task of finding a partner to venture into domestic supply.

He thought the domestic gas market was going to be opened up on the same pattern as the I and C sector with the regulator creating space for a multiplicity of largish players.

British Gas learnt its lesson from its experience with I and C, where it lost nearly three-quarters of its customer base.

'It lobbied hard so that wasn't repeated. The incumbent was allowed to react much more quickly and forcibly. All credit to British Gas. They have delivered significant achievements: electricity, Goldfish and now home services, which will be important to ensure their churn rates come down. Not only do they get a profits stream but they get high retention rates.'

While at Calortex, Franklin often demanded action from the regulator to curb potentially anti-competitive behaviour by British Gas.

He does not expect the regulator to force the energy giant to relinquish any of its customer base but sees the new Competition Act as a check on any abuse of dominant position.

For the time being he will be watching developments in the domestic energy market from the sidelines (though as current president of the Society of British Gas Industries his involvement remains more than academic).

There is plenty to observe in a deregulating Europe, and plenty of opportunity for a man who has lost none of his appetite for adventures in the competitive marketplace. ■