

# Morning Meeting Note

## The Investext Group

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07:21am EDT 15-Aug-01 Bear Stearns (K. Winters,R./D. Franson,R. 212 27) ENE  
ENE: Man Overboard! What About The Ship?

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8/15/01

Subject: Company Update  
Industry: Wholesale Energy

BEAR, STEARNS & CO. INC.  
EQUITY RESEARCH

ENRON Corp. (ENE 42.93) - Attractive  
Man Overboard! What About The Ship?

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Data

Last ROE 10.8% Dividend/Yield \$0.50/1.19% Market Cap (MM) \$38.3  
Billion  
52-Wk Range \$91-\$42 Shares Out 891 Million Avg Day Trade Vol 4.09 MM

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Key Points

\*\*\* Enron announced late Tuesday that Jeff Skilling had resigned as Enron's President and CEO citing personal reasons. As shares of the company have fallen approximately 50% since January, we believe this unexpected announcement raises significant concerns with regard to the future direction of the company. We reiterate our Attractive rating for Enron.

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	Earnings Estimates				Year	P/E	Consensus	
	Q1 Mar	Q2 Jun	Q3 Sep	Q4 Dec		Year	Cur (Q3)	Year
2000	\$0.40	\$0.34	\$0.34	\$0.41	\$1.47	29.2x		
2001	\$0.47	\$0.45			\$1.80E	23.9x	\$0.43E	\$1.82E
2002					\$2.15E	20.0x		\$2.16E

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AN UNEXPECTED RESIGNATION

Enron announced late yesterday that its Board of Directors had accepted the resignation of Jeffrey K. Skilling as Enron's President and CEO. Skilling will continue to serve as a consultant to Enron and its Board of Directors. Kenneth L. Lay, currently Enron's chairman of the board, will assume the additional responsibilities of President and CEO and has agreed to extend his employment agreement with the company through the end of 2005. Lay served as Enron's CEO from 1985 until Skilling's election earlier this year.

UNSETTLED QUESTIONS ABOUND

Given his ambitious nature and the years spent being groomed for this position, Jeff Skilling's utterly unexpected resignation raises tremendous questions. While we are loathe to speculate on what may indeed be a completely personal matter, the suddenness of this announcement is sure to raise substantial concerns among investors. Again, while we don't wish to presume and/or speculate into the reasons for Jeff Skilling's departure, it is extremely noteworthy to mention that the board accepted his resignation and followed the

strict terms of his contract and opted not to offer him any type of severance package. (Skilling's contract stated that if he was to voluntarily resign as CEO, he would forfeit all rights to his severance package)

There has and now there continues to be numerous questions regarding the aggressiveness of both the operational and financial aspects of Enron. Ranging from complaints of a lack of visibility within Wholesale Energy to a now decimated Broadband Services, Enron has fought a losing PR battle throughout the first half of 2001. Although Ken Lay insists that nothing will change with regard to the company's business strategy, focus, and direction, yesterday's decision will certainly not be regarded as the type of announcement designed to engender confidence with investors.

#### RETURN ON CAPITAL EMPLOYED - WHO'S IN CHARGE?

Enron is clearly an organization filled with many motivated and intelligent people. There is little disagreement that the creative juices flow freely within the company, however, while the creativity and successes of Enron have been widely applauded by analysts, investors, and Enron alike, the failures of the company have also been large and costly. The turnover in the organization, changes in direction, and the exiting of failed business areas, are often quickly dismissed by the company as a small price to pay for the dynamic nature of a company such as Enron. However, as we have mentioned repeatedly over the past nine months since our initiation of coverage of Enron, the returns achieved by the company (whether they are measured by return on capital employed or simply operating margins) fall very short of the types of returns that Enron publicly aspires to achieve, as well as the types of returns that would justify the generous valuation that the company has carried in the past and continues to carry (especially relative to its peer group).

Jeff Skilling's self-described main role as President and CEO was to improve returns within the overall organization up to a level commensurate with the world's leading companies. Is this still the goal for the organization? Will Ken Lay have the same focus to drive returns up to these higher levels and how large are the obstacles - which we have previously outlined - that Enron must overcome to improve overall returns? While there has been no change to earnings projections by the company, nor have we made any changes to our estimates at this time, we believe that the unexpected resignation of Jeff Skilling will raise concerns amongst investors that deep problems and negative issues lurk in the future.

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