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CEO/COMPANY INTERVIEW

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Enron Transportation Services (ENE)



DANNY J. MCCARTY is Managing Director and Chief Commercial Officer of Enron Transportation Services. He began his career in the energy industry in 1982 when he joined K&E Petroleum, Inc., an oil and gas exploration and acquisition company as Vice President - Legal. In 1987, Mr. McCarty joined the law offices of Jack Graves as an Associate Lawyer in the energy practice. In 1988, he joined the legal department within Enron Interstate Pipeline Group focusing on take-or-pay litigation, gas supply and

gas marketing. Mr. McCarty joined Enron Capital and Trade Resources in June of 1991 as a Director of Enron Power Services, Inc. and was promoted to Vice President in January 1994 responsible for independent power producer marketing. In April 1995, he assumed responsibility for ECT's strategic acquisition efforts internationally together with ECT's Non-European regional development activities. In August 1996, Mr. McCarty relocated to London and was appointed Managing Director of Enron Europe in January 1998. He completed his undergraduate work at Columbia University (NYC), and University of Nebraska and Lincoln and received his BA in 1978. He also attended University of Nebraska School of Law where he received his JD in 1981, and is currently a member of the State Bars of Nebraska, Kansas and Texas.

SECTOR –ENERGY

(LAS627) TWST: Could you provide our readers with a brief overview of the company?

Mr. McCarty: Enron Corp. is a multinational energy company, focusing on energy and telecommunications worldwide. Just some examples of what we do — we have an extensive fiber-optic network throughout the United States. We're a leader in trading bandwidth throughout the United States. That expertise stems from our trading expertise developed in the United States in primarily gas and electricity. But that has been expanded to include oil, gas, petrochemicals, steel, and all types of metals through the acquisition of MG in Europe at the end of last year.

We have significant operations in Europe through the London office. The London office trades extensively in gas, electricity in the UK and on the Continent. They're the market maker in the Nordic markets in electricity trading. We continue to develop power projects throughout the world. We have current power projects in such places as India, Turkey, the UK, and Italy, throughout the United States. Sixty million dollars-plus is our market cap today. I think that's based on a 50-plus p/e statistic.

I guess that's kind of a brief overview. Kind of the genesis of Enron was back in the 1980s, 1982 through 1986, when there was significant consolidation of pipeline capacity in the United States. Enron was actually the result of

mergers between Northern Natural, FGT, and Houston Pipeline, creating the largest pipeline network in the United States. So that was really the genesis of it. And from that, it was merely starting to transfer skill sets from one area to the other, from jurisdictional to nonjurisdictional, (from jurisdictional activities such as terra-based transportation services to non-jurisdictional such as trading). That's how we became what we are today.

TWST: Focusing on Enron Transportation Services, what do you see today as the overall business and company aspects of that subsidiary?

Mr. McCarty: Let's start off with what Enron Transportation Services is today. We either own, control, or both, four major interstate pipelines. First is Northern Border. We own about 10% of Northern Border and operate that. That pipeline brings Canadian gas down into the Chicago area. Then we have Florida Gas Transmission. That runs from the state of Texas to the tip of Florida and is the only transporter of natural gas into the state of Florida. Then there's Transwestern Pipeline, which runs from the state of Texas to the California border at Topock and Needles. That goes into the southern part of California right where the California border meets the tip of Nevada. Then we have Northern Natural, which is a pipeline that today begins in Texas and flows north into the market area in and around Ventura or the Chicago area. So that's kind of the asset ownership of Enron Transportation Services.

Most recently, we changed our name from the Enron Gas Pipeline Group to Enron Transportation Services. And the reason we did that was because we've been undergoing somewhat of a metamorphosis to start focusing on really more transportation services and/or intellectual capital, rather than merely focusing on operation

of the physical asset. And with that, really what we're doing today is we're looking at services. We're one of the largest transporters of natural gas in the United States. We transport about 9 bcf of natural gas a day on the 25,000 miles of pipe that constitute our network. That gas is distributed into 21 various states in the West, Midwest, Gulf Coast, Southeast markets.

At this point, we are transporting for shippers and providing them various storage services so that they can accommodate their own needs. Each customer has a various set of needs. For example, you may have a co-generator out there with a simple cycle gas turbine. What he's really going to want to do is take as much gas in a particular hour so he can hit the peaks and sell his electricity for the highest price possible. When the electricity prices then fall, he doesn't want to take any gas, right? So he's going to have a completely different set of needs from a local distribution company that has relatively constant requirements and may even have some of their own peak shaving on their system.

Each customer now has a different set of needs. We're getting our people out there to start understanding these needs. It's a big issue in the industry, particularly in the electricity industry because, historically, pipelines have not been very responsive to the electricity industry and the need to be able to accommodate the ebbs and flows of the demand in electricity, i.e., the peaks and the valleys.

TWST: Could you give us an idea of what's on the agenda for that area over the next 12-24 months?

Mr. McCarty: Typically, the public and the media don't see a pipeline's future development or expansion plans, because they're kept internally from a pipeline standpoint. It's not just

Enron. It's any big pipeline out there, whether you're talking about Williams or El Paso. We constantly have pipeline expansion efforts under way in-house that are not made public. We don't make them public because it takes so much time to do the engineering and a number of other things. You have to start anticipating market needs. So for the past several years, we have been looking at a number of things that we can do in the market today. Let me just take Transwestern, for example. Transwestern — last year, we did an expansion that effectively brought in 140,000 in mmBtu per day into the California market.

But still we've seen a lot of tightness in that market and in fact an inability to be able to get enough gas into the state to forego any of the brownouts or blackouts that we've been experiencing over the last three or four months or so. But effectively, what we're trying to do is be out in front of the market, then together with our pipeline capacity and El Paso's pipeline capacity coupled with proper management of the storage in-state in California by the electric utilities, keeping in mind we don't control any of the storage capacity in that state. They do. There should be sufficient pipeline capacity even this year to avoid blackouts/brownouts. Now that being said, there's going to be a lot more demand growth over the next few years. But we're planning the expansion of our pipeline, which will be a twinning of that line and expect to see that in service by 2003.

In a lot of areas — and California's just the easiest example because it's something that's been in the forefront of the news — our pipeline ran full all year in the state of California. El Paso's pipeline did not run completely full all year and there was one outage that resulted from an explosion. But the shippers were not shipping gas all year into that state filling up their storage. If that storage would have been full, I

would venture a guess to say there probably would not be the frequency of blackouts you're seeing today. People that control that storage made a market call. They saw what happened over the past four to five winters during mild winters where they actually paid money to put gas in storage and got no benefit from that gas in storage because the winters were so mild. So here, this winter comes around. It's not a mild winter. They were caught off guard. So it wasn't necessarily what I would consider lack of pipeline capacity going into that state.

You could say the same thing for some of the other areas. But a lot of the other areas throughout the United States manage their storage capability a little bit better. We're not seeing problems with electricity capacity. I would say over the next five years, what we'll see is significant growth in the electricity industry. Most of that growth is going to be marginal electricity and the fuel that's on the margin is gas. It's not going to be coal. I know that if you wanted to build a coal plant today, and you started from scratch, you would be looking at a six- to 7-year horizon to bring that on. That means natural gas is the way to go.

The good news is that most natural gas is transported on interstate pipelines governed by FERC. That's pretty much all — I mean, FERC has always governed pipelines. They understand pipeline expansions. They understand the necessity to bring pipelines on relatively quickly and have been responsive to that in the past. I'm sure they're going to be very responsive to it over the next two to three years. Now whether that gas can get to particular delivery points and then be delivered into states with the same ease, that's another question. Because when a hit state — for example, when our gas on Transwestern hits California, all at once the governing of the construction of a

pipeline or the construction of a power plant or the construction of an overhead transmission line is now subject to the California PUC or a state PUC. I can't guarantee states will move as fast as the federal government will. That could create some bottleneck constraints down the road.

I guess the next area that we probably need to talk about is whether there is adequate gas supply. If I build pipeline capacity to the state of Florida like I'm planning to do, if I build pipeline capacity to the state of California, like I plan to do, is there sufficient gas supply to fill that pipe up for the foreseeable future? I guess the short answer to it's "yes, there is." The longer answer to it is "well, where's it coming from?"

We have significant drilling activity going on in the Rockies. Pipelines though don't tend to flow Rockies' gas south then west into California. That just means we're going to have to change the flow of some pipelines. But we can get it there. There's sufficient pipeline capacity today to get a significant amount of Rockies' gas into California.

The other area clearly would be from Canada and eventually from Alaska. There are pipelines like our Northern Border pipeline and some of the other pipelines that have recently been built will bring that capacity back. But what we've seen is, if you change a hub point or a major gas point, like Ventura, and either short that point by half a bcf or put an additional half a bcf to that point, it changes gas flows throughout the United States. So we're getting a very responsive pipeline network that's able to get gas that's needed to the areas that will pay for that gas. So I'm not too concerned about the availability of gas throughout the supply basins.

TWST: What's in the industry today? Is there much consolidation or merger and acquisition activity for strategic purposes?

Mr. McCarty: Tremendously. We've seen El Paso, in particular, come in and gobble up pipelines like ANR, Coastal, and Sonat. Those were major interstate pipelines and they've all been consolidated under the El Paso umbrella. And Duke/Williams likewise is doing the same thing. So whereas there used to be 10, 15 major pipelines out there, I think if you end up with three pipeline presidents at the table, one from El Paso, one from Duke/Williams and one from Enron, you cover probably 60%, 65% of the interstate capacity.

TWST: Do you have any overall thoughts on the regulatory environment and the payoff between environmental and industrial needs and consumer needs over the next five years or so?

Mr. McCarty: My feeling is that in certain areas the pendulum has swung all the way over to the environmental side in a number of areas, particularly on the state side, if you're looking at California, for example. But I think the pendulum is going to come back. But there's going to be proper deference to the environmental concerns. That being said, I tell you though, when you're having a crisis like you're having in California today, if you need to construct power plants, overhead lines, intrastate gas transmission lines, and interstate gas transmission lines, I know from my standpoint, on the interstate gas transmission lines, I intend to ask for expedited certificates from FERC and I know they're going to respond. Now I haven't talked to anybody specifically at FERC to see if they would support me on that, but they're pretty responsive. They are not going to allow people in a region or an entire state to suffer brownouts and blackouts because of bureaucratic red tape.

TWST: Thank you. (DA)

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