CATALYST
ENERGY SOLUTIONS

Energy Element / April 2014

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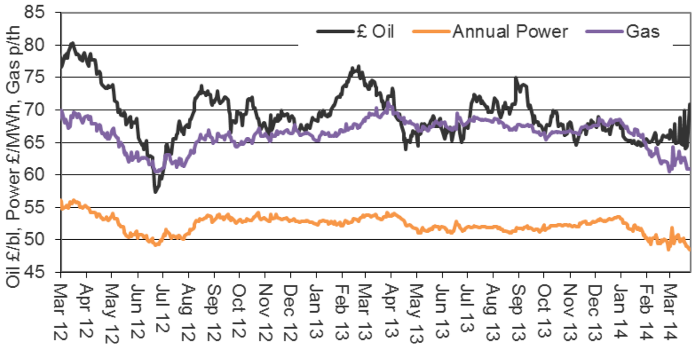
Crimea tensions fail to halt continued slide

Despite gas and electricity prices surging 10% on 3 March following heightened tensions in Crimea, gas and power prices fell over the month as the threat of conflict diminished. But increased volatility characterised March from this point onwards.

Overall, economic fundamentals of low demand and high supply continued to weigh on gas prices. These falls fed into power contracts, with annual April 14 power down 1.1% over the month to £49.4/MWh.

Crude oil and annual wholesale gas and power prices



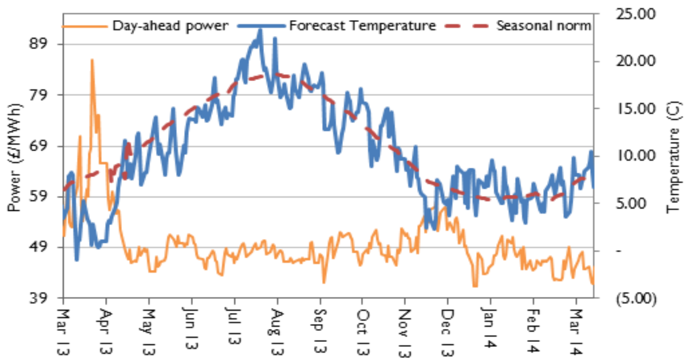
On the commodity front, monthly average Brent crude oil dropped 0.8% to $107.7/bl with fears of an economic slowdown in China and warmer weather returning to the US. The contract fell to a four-month low of $106.0/bl on 20 March. Carbon prices fell 5% to average €6.2/t as the contract tumbled towards the end of the month, dropping to a six-month low of €4.27/t on 28 March. Coal prices fell 0.8% to average $81.0/t for the month. Lower demand in China and developing economies influenced the fall.

Bearish trends continue for gas as March sees wind generation records

In March, short-term gas prices continued reductions seen since the start of the year. Russia/Ukraine tensions saw the day-ahead contract rise 10% to 61p/th on 3 March. However, strong supply data, with storage capacity 55% full, offset these early gains. The contract dropped 4.7% over the month.

Short-term power contracts dropped following reductions in gas prices and record wind generation over the month. Wind generation peaked at 13% of the generation mix on 20 March. The day-ahead contract fell 1.7% month-on-month to average £44.5/MWh. Spot power prices were also influenced by record wind generation.

Spot power prices and temperatures



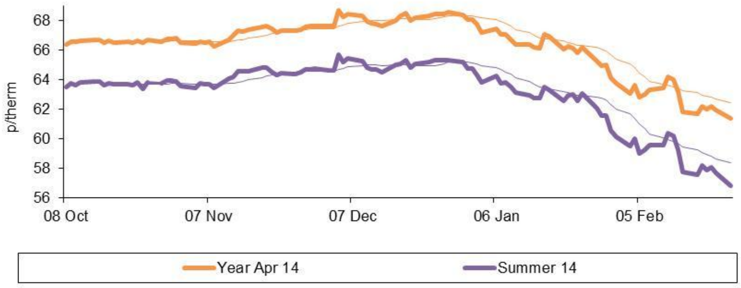
Russia out in the cold as carbon frozen

Western sanctions have already started against Russia and continue to underpin the gas market. A cut-off of supplies from Russia is unlikely. High gas storage levels following the mild winter mean if supply restrictions occur the impact would be limited.

It was announced in the Budget on 19 March that the rate of carbon price support would be frozen at £18/t from 2016. The move should see power prices fall along the curve with lower costs for coal and gas burn.

Catalyst Commercial Services’ independent approach enables clients to manage their exposure to energy price risk, while at the same time benefiting from a first class service from a range of major and independent suppliers. Catalyst Commercial Services’ procurement solutions make it simple, so contact a member of the team to discuss requirements.

Annual gas prices



Annual gas prices fell in March with economic fundamentals of low demand and high supply keeping the market long for most of the month.

Annual April 2014 gas prices dropped 1.3% to 61.6p/th over the month.

The summer 2014 contract decreased 2.3% to a monthly average of 57p/th. The contract fell to a record low of 53.2p/th on 28 March.

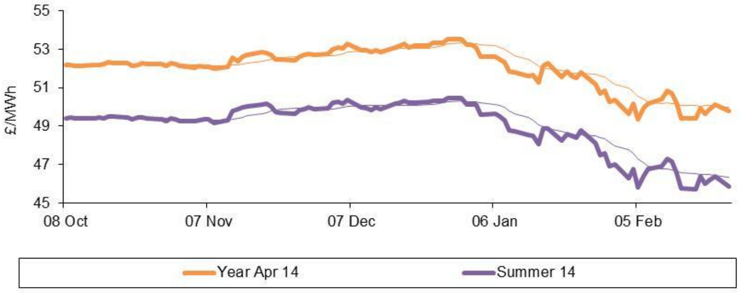
Spot gas prices

Spot gas prices declined in March despite the price spike at the start of the month, caused by escalating tensions in Russia/Ukraine.

Day-ahead gas prices fell to a two-year low of 50.65p/th on the 24 March and averaged 56.7/th over the month.

Month-ahead gas prices were down 3% to a monthly average of 57.2p/th.

Annual power prices

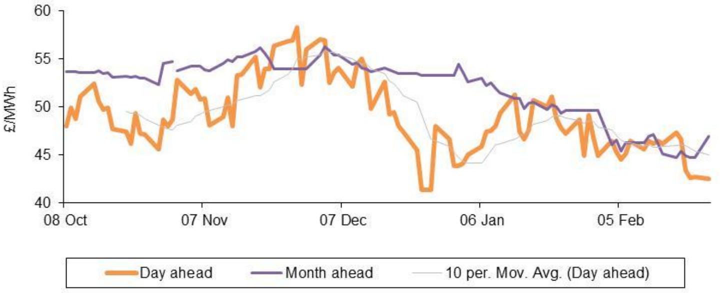


Annual electricity prices decreased, tracking falls in their gas counterparts.

Annual April 2014 power lowered 1.1% to a monthly average of £49.4/MWh.

The summer 2014 contract fell 1.9%, falling to a record-low of £42.7/MWh on 31 March, its last day of trading.

Spot power prices



Day-ahead power prices dropped month-on-month because of record wind generation pushing more expensive gas off the system. Gas-fired power generation in the UK fell to a 17-year low last year, according to figures released by DECC in March.

Day-ahead electricity prices fell 1.7% to an average of £44.5/MWh. The contract reached an 18-month low of £41.10/MWh on 27 March.

Month-ahead power prices dropped 3% to average of £46/MWh.

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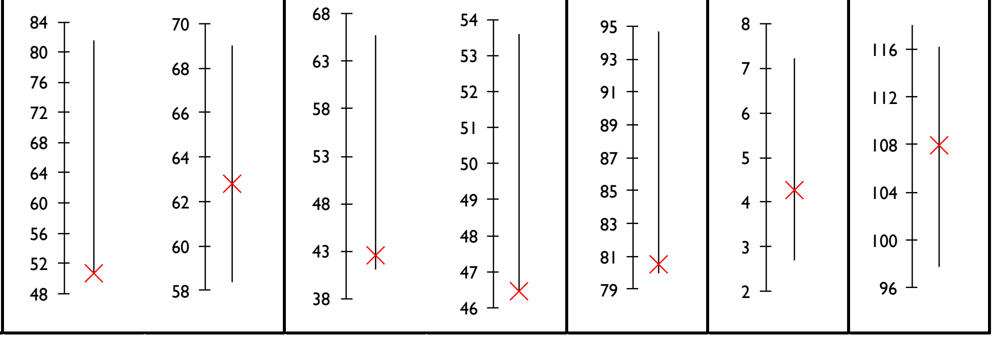
Key market indicators: 31/03/2014

		Gas (p/th)		Electricity (£/MWh)		Coal	Carbon	Brent crude
		Day-ahead	Year-ahead	Day-ahead	Year-ahead	($/t)	(€/t)	($/bl)
March	31 Mar 14	50.65	62.80	42.50	46.45	80.50	4.27	107.90
February	28 Feb 14	56.45	60.85	44.75	48.98	80.50	6.70	108.65
Last year	1 Apr 13	71.00	68.70	65.75	54.03	92.85	4.95	109.53
Year-on-year % change		(29%)	(9%)	(35%)	(14%)	(13%)	(14%)	(1%)
Year high		81.50	69.03	65.75	53.60	94.65	7.22	116.17
Year low		52.50	58.38	41.10	47.00	80.00	2.70	97.70
This table shows the price at the end of this month compared with prices from the previous month and year. The graphs show the position of this month's prices with a red X and the range of prices over the year is represented by the black line.								



Commodities

Carbon: EU Emissions Trading Scheme carbon is quoted as over-the-counter (OTC) latest opening prices. All carbon prices are in euros per tonne (€/EUA).

Coal: Coal is quoted as OTC latest opening prices. All coal prices are in US dollars per tonne ($/t).

Electricity: UK power base-load and peak-load are quoted as OTC latest opening prices. All UK electricity prices are in pounds per megawatt hour (£/MWh).

Gas: UK National Balancing Point (NBP) gas is quoted as OTC latest opening prices. All UK gas prices are in pence per therm (p/th).

Oil: Brent crude oil is quoted as OTC latest opening prices. All Brent crude oil prices are in US dollars per barrel ($/bl).

Language/ terms

Bearish: A bearish market shows a general decline in prices over a period of time.

Bullish: A bullish market shows a general increase in prices over a period of time.

Curve: A graph of forward prices over a future time period.

Margin: The indicated UK imbalance of a given settlement period. It is the difference between the sum of the indicated generation available, and the national demand forecast made by National Grid.

Over-the-counter (OTC): The trade of a commodity directly between two parties, often on standardised terms.

Spark/ Dark spread: The theoretical net income of a gas-/ coal-fired power plant from selling electricity having purchased the necessary fuel. The clean spark/ dark spread is this net income adjusted for the cost of carbon.

Energy market likely to face competition investigation

Ofgem has proposed to refer the energy market for an investigation by the Competition and Markets Authority (CMA), following an assessment of its present state that revealed a number of concerns.

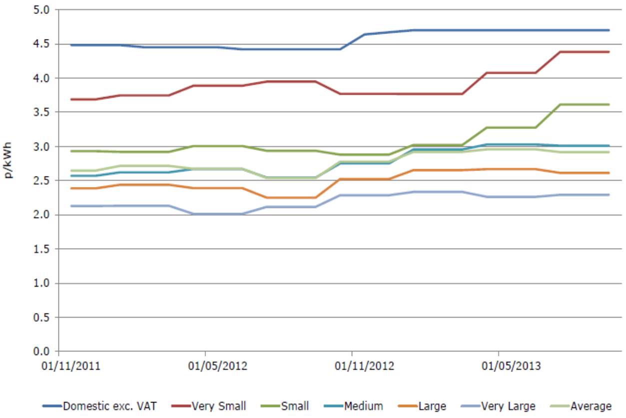
Profits increasing

The regulator, alongside the CMA and the Office of Fair Trading, issued on 27 March its *State of the Market* assessment.

The report found that average profits for the Big Six increased from £3bn in 2009 to £3.7bn in 2012. Given there was no clear evidence of increased efficiency from suppliers, Ofgem claimed the increases could be indicative of a lack of effective competition.

The report also noted that there was continuing uncertainty over whether the vertical integration of the large energy companies was in consumers' interests. It further highlighted weak competition between larger energy suppliers, low customer trust and engagement, and barriers to entry and expansion for new suppliers.

Average domestic and non-domestic gas prices (p/kWh)



Source: Ofgem

Small businesses pay more

The market for business consumers is more competitive than the domestic sector – given many companies are able to engage effectively with suppliers, either directly or through a broker. But Ofgem raised concerns that micro-businesses had lower engagement and satisfaction with the market when compared to larger companies. The regulator said that average gas prices paid by non-domestic customers of different sizes were highly correlated (*see chart above*) but that there was a consistent price difference, with larger customers paying lower rates than smaller businesses. This, Ofgem suggested, might be a consequence of economies of scale and the fact that larger companies bear more of the risk of changes in wholesale prices. But the higher prices paid by smaller businesses might also be evidence of less active competition, the regulator said.

The assessment concluded that an in-depth review of the market was needed, and confirmed Ofgem issued a consultation on the proposal on the same day. Views are sought until 23 May.

Retail margins are just one of a trio of factors pushing up bills, alongside government green levies and rising global fuel costs. Nonetheless, attempts to ensure the market is working for consumers should be welcomed.

Ofgem

Ofgem plans to double power cut compensation

Electricity distribution companies could be forced to double compensation payments made to customers cut off in severe weather. Ofgem's proposed change follows storms late last year when around a million consumers lost power supplies.

Under the regulator's plan, published on 1 April, distribution network operators would be required to pay out £70 a customer if they failed to meet minimum levels of service – up from the current level of £35. This compensation would be paid after an initial loss of supply lasting for 24 or 48 hours – depending on the category of the severe weather event. Consumers would then receive £70 for every 12-hour period without power. The current cap on compensation per customer, per event could also increase from £216 to £700. Ofgem is seeking views on its plans until 30 May. It expects to publish its decision by 1 July.

Ofgem

Budget confirms carbon tax cap

Chancellor George Osborne confirmed at Budget 2014 a series of measures to reduce business energy costs and to ensure "the UK remains a competitive location for manufacturing". The headline announcement for the energy sector was that the government would cap the UK carbon tax, known as the Carbon Price Floor (CPF).

Carbon tax frozen

The CPF aims to provide power generators with an incentive to invest in low-carbon technologies by increasing the price of carbon and therefore the cost of power generated using oil, coal or gas. But following concerns that British businesses were paying more for electricity than their European counterparts, Osborne set out plans to cap the rate at £18/t from 2016-17 up to the end of the decade. The government said that this move could save British businesses up to £4bn by 2018-19. The government also pledged to review the CPF trajectory for the 2020s and to consider a further cap on the rate.

More compensation

Osborne also announced that the government would extend its compensation package for energy-intensive industries for the costs of the CPF and the EU Emissions Trading Scheme to 2019-20. Subject to approval from the European Commission, the government will also introduce a new compensation scheme to help the manufacturing sector cope with costs arising from the Renewables Obligation and the small-scale feed-in tariff scheme – both of which aim to encourage investment in renewables generation.

The Climate Change Levy (CCL), which is paid on energy used for lighting, heating and power by businesses and the public sector, will increase in line with inflation from 1 April 2015. To ensure the most energy-intensive businesses remain competitive, the government reiterated its commitment to introduce exemptions from the CCL for energy used in "metallurgical and mineralogical" processes from 1 April 2014. An exemption from the Carbon Reduction Commitment scheme for the UK's most energy-intensive industries will also be introduced.

This Budget focussed on the affordability of energy for the UK's most energy-intensive businesses, providing little support for smaller businesses and households, which are also feeling the pinch from increasing energy costs.

Treasury

Small businesses "need increased market protections"

The government should give small businesses the same level of consumer protection when drafting legislation as domestic customers, the Federation of Small Businesses (FSB) has said.

In its *Small Businesses as Consumers: Are They Sufficiently Well Protected?* report, published on 12 March, the FSB claimed that many small businesses were disadvantaged when compared with both large businesses and domestic consumers, when they took out a contract with a new energy, telecoms or water provider. The study noted that most small businesses did not have staff with a specific procurement role, which meant that they lacked the time and knowledge necessary to make informed purchasing decisions. Smaller businesses also had far less bargaining power than larger firms, the report said. The FSB said utility suppliers should be required to publish their default tariffs for smaller business customers and that all regulators should have the ability to protect businesses from mis-selling.

Separately, on 28 March Labour leader Ed Miliband pledged to deliver stronger energy market protections for small companies. Miliband said it was "unacceptable" that small businesses did not have the same basic protections that were available to households. According to the Opposition leader, if elected in 2015, Labour would give its proposed new regulator the power to prevent suppliers from employing auto-rollover contracts and would limit back-billing to one year.

FSB Labour

CRC Phase Two begins

Phase Two of the Carbon Reduction Commitment (CRC) energy efficiency scheme, which runs up to 2019, began on 1 April 2014. It offered participants the opportunity to purchase cheaper allowances for surrender in the 2014-15 compliance year.

Buying early

The CRC is a mandatory emissions trading scheme aimed at reducing carbon emissions from large commercial and public sector organisations. Organisations mandated to participate in the CRC must monitor their emissions and purchase allowances to cover their energy use.

CRC allowances will be sold in two fixed price sales in each CRC compliance year: a forecast sale of £15.60/allowance and a retrospective compliance sale at £16.40/allowance.

The forecast application period for the first compliance year of Phase Two takes place between 1 April and 30 April. Forecast payments will be made between 1 June and 20 June with the allocation of allowances taking place between 1 June and 15 July.

Buy-to-comply

If participants are unable to forecast allowances, they can retrospectively apply for allowances at the end of the compliance year – between 1 June and 31 July 2015. These allowances will be charged at the higher rate of £16.40. Allocation of these allowances will be made between 1 September and 15 October 2015 and payments will be made between 1 September and 19 September 2015.

All allowances purchased must be surrendered by 31 October 2015.

The final allowances for the First Phase of the CRC will also have to be paid for in September 2014. These will be priced at £12/allowance.

Businesses looking to save money under the CRC should consider buying allowances in the cheaper forecast auction.

Environment Agency

Cross-sector regulators network launches

The UK Regulators Network (UKRN) was launched on 19 March.

The UKRN brings together the UK's economic regulators, including Ofgem, Ofwat and the Financial Conduct Authority, to improve co-ordination with the aim of enhancing investment and efficiency for consumer benefits.

The network aims to provide a vehicle for co-operation that supports the separate regulatory frameworks of the individual regulators. It will allow them to work together on cross-sector issues and learn lessons across their industries to improve regulation and the promotion of competition to secure better outcomes for consumers.

The three main objectives of the network are to: improve the consistency of economic regulation across sectors; deliver efficient regulation; and improve the understanding of how economic regulation works in the interests of consumers, markets, investment and economic performance.

The UKRN's first areas of focus will include: facilitating efficient multi-sector investment projects; promoting customer engagement and switching in regulated markets; assessing cross-sector resilience and cyber-security; and developing a clear understanding of the overall affordability of regulated services for consumers.

Ofgem

E.ON UK to end automatic contract roll-overs for business customers

E.ON UK has become the first major supplier to end the automatic contract roll-over process for new and existing business customers.

In a statement on 28 March, the company said the move was another step towards "simpler and fairer" energy deals. E.ON UK's own research found that 86% of small businesses preferred to negotiate new contracts or move to a more flexible agreement rather than being automatically rolled on to a new long-term fixed price deal.

Director of business energy Anthony Ainsworth said that E.ON UK would allow customers to either renegotiate a new deal or move them on to its cheapest variable tariff rate with no exit fee. He added that the move would provide the greatest consistency and transparency across pricing and contracts.

E.ON UK

RWE npower small business customers to benefit from new bill design

RWE npower announced on 17 March that its small and medium enterprise (SME) customers would soon benefit from simpler billing for their electricity.

The company's new bill design will provide "at-a-glance" visibility of account balances, payments and charges, and will incorporate design elements such as colour-coding, sign-posting and itemised groupings clearly to provide SME customers with information. Important account information has been given greater prominence for ease of reference, while "unnecessary and confusing information" has been removed.

RWE npower said its research indicated that its new approach to billing and information would help small businesses actively engage in managing their energy. Nearly half of respondents to a company survey said the new bill design would also positively influence their perceptions of npower as a more "modern, customer-focused company".

RWE npower

National Grid confirms 2013-14 triads

National Grid has published the dates and times of the 2013-14 triads. Triads measure maximum demand readings three times a year and use the average of these readings to calculate Transmission Network Use of System (TNUoS) charges. For winter 2013-14 the Triads are on 25 November, 6 December and 30 January in each case between 17:00 and 17:30. The highest half hourly demand was on 25 November at 50,694MW.

Triad charges are only applicable for half-hourly metered sites. Typically, these costs will be bundled in to electricity charges but some larger customers may opt for a "pass through" arrangement that reconciles their actual triad use against a forecast.

National Grid

Centrica warns on UK dependency on gas imports

Allowing energy security to become a "forgotten priority" could leave the UK relying on imports for up to 70% of its gas needs by 2020, according to Centrica chief executive Sam Laidlaw.

Speaking at a conference in the US on 5 March, Laidlaw said that UK gas production was falling rapidly, with North Sea oil and gas output dropping 38% in the last three years. Events in Ukraine during March had, he argued, provided a "sharp reminder of where our priorities should lie". With 80% of UK buildings heated by gas, the country must look to diversify sources, and shale gas could contribute significantly to the UK's future energy mix, Laidlaw added.

Laidlaw noted that around 3.7GW of coal-fired generation was expected to be shut down by the end of next year, and he urged policy-makers to address security of supply concerns with "a new sense of urgency". He said that investment in new power generation in the UK had slowed sharply owing to political uncertainty, which has intensified further following Labour's pledge to freeze energy prices if elected in 2015.

Centrica