Energy Element / May 2012

CATALYST ENERGY SOLUTIONS

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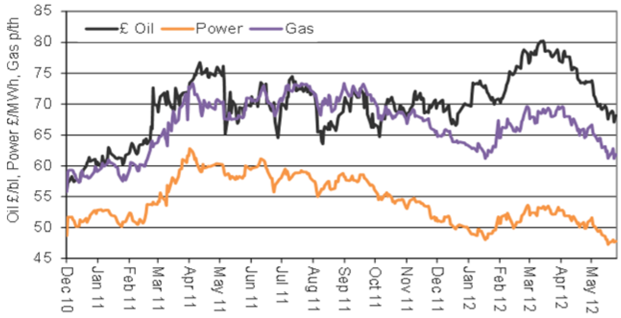
Deepening eurozone crisis sees energy prices plunge

The fallout from the Greek elections renewed eurozone instability fears during May, forcing GB wholesale energy prices to drop and international energy markets to reach new lows.

Annual coal hit a 20-month low of $98.8/t on 24 May on continuing weaker demand from the Far East, while the same day month-ahead Brent crude oil slipped to a five-month low of $105.6/bl. Carbon also struggled to bounce back after recent record lows. These factors helped drag annual gas and electricity prices down.

Crude oil and annual wholesale gas and power prices



On average the annual October 12 gas price lost 5% during May and bottomed out at 61.2p/th on 24 May. Annual October 12 baseload electricity price saw a 4% drop over the month, reaching a two-year low of £47.25/MWh on 18 May. Prices for annual gas and electricity are now 9% and 18% lower respectively than they were a year ago. Gas and power prices have only fallen to these levels once in the past 12 months—in January when a mild winter drove prices below 65p/th and £50/MWh.

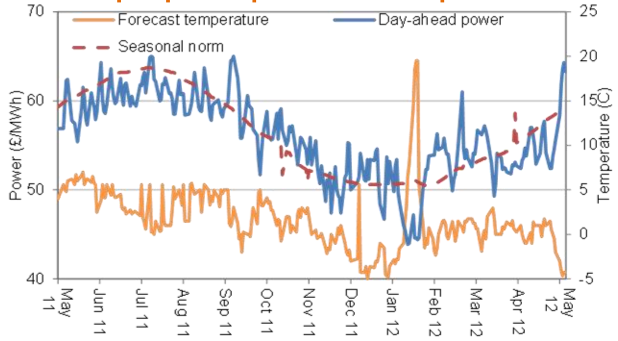
Warmer weather erodes short-term contracts too

Short-term prices were similarly affected by falling oil and coal contracts. But lower demand, spurred by the warmer weather, also helped to suppress prices in May.

Day-ahead gas dropped to a four-month low of 53.1p/th on 28 May and averaged 57.5p/th over the month. Prompt prices have now fallen 13% from the peaks seen in February and March.

Baseload electricity on the day-ahead market also fell to a five-month low of £40.0/MWh on 28 May. The short-term price averaged £44.0/MWh in May, which is 17% below the peak in February. But this is still £2/MWh more expensive than the £42.0/MWh low seen in January.

Spot power prices and temperatures



Prices could reduce ahead of summer

Some traders believe continuing low coal prices will encourage generators to use coal-fired stations as much as possible this summer, keeping near-side power prices low. This driver could be accompanied by a continued fall in oil prices if economic uncertainty continues. Lower oil prices should also continue to act as a drag on gas.

But prices will remain volatile as the EU continues to compete with high Asian demand for LNG and geopolitical events in the Middle East show no signs of easing.

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. Our procurement solutions make it simple, so contact a member of the team on 0870 7107560 to discuss your requirements.

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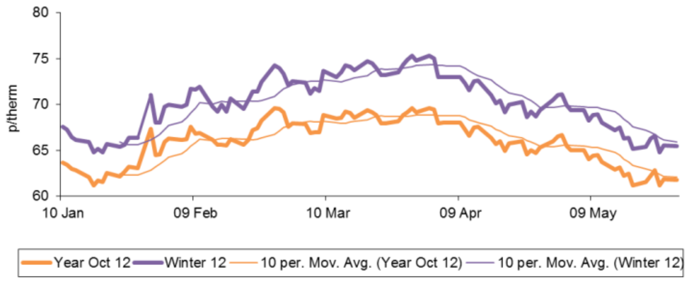
Annual gas prices

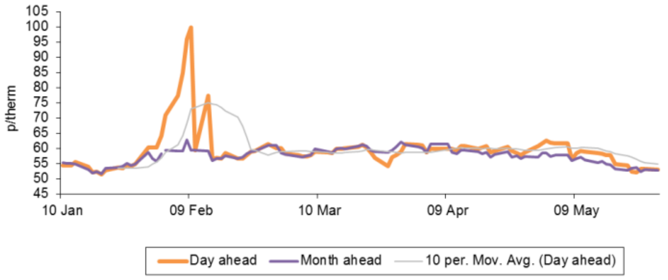


Annual gas prices saw downward movement over the month following falling oil prices.

Annual October 2012 gas prices dropped to a four-month low of 61.2p/th on 24 May.

The winter 2012 contract dropped 5% to a four-month low of 64.8p/th on 24 May.

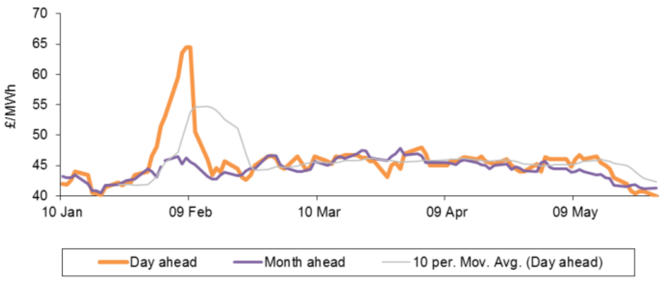
Spot gas prices



The month-ahead gas price fell to 52.5p/th on 24 May.

Day-ahead prices dropped as warmer weather arrived and demand decreased, reaching a four-month low of 53.1p/th on 28 May.

Annual power prices

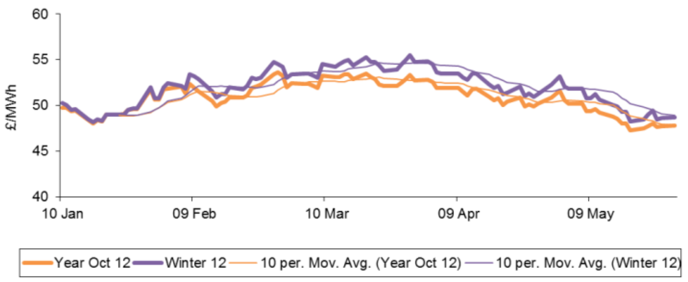


Annual electricity prices also saw notable falls following their gas counterparts.

The annual October 2012 baseload electricity dropped 4% over the month and reached a two-year low of £47.2/MWh on 18 May.

The winter 2012 electricity contract dropped to £51.0/MWh on 24 April.

Spot power prices



Short-term contracts dropped as a result of rising temperatures and cheaper coal-fired generation.

Day-ahead electricity prices reached a five-month low of £40.0/MWh on 28 May.

Month-ahead power prices fell to £41.3/MWh on 28 May.

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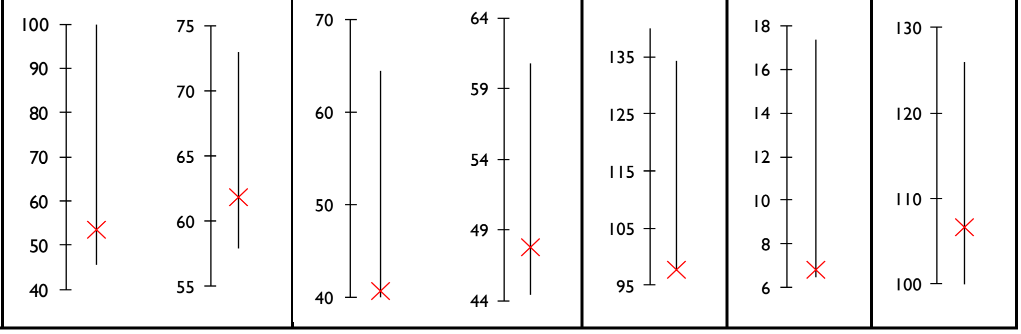
Key market indicators: 25/05/2012

		Gas (p/th)		Electricity (£/MWh)		Coal	Carbon 2012	Brent crude
		Day-ahead	Year-ahead	Day-ahead	Year-ahead	($/t)	(€/t)	($/bl)
May	25 May 12	53.40	61.85	40.75	47.75	97.65	6.80	106.55
April	25 Apr 12	58.65	65.03	44.50	50.10	110.35	7.18	118.48
Last year	26 May 11	58.00	67.90	50.50	58.38	126.50	16.45	114.64
Year-on-year % change		(8%)	(9%)	(19%)	(18%)	(23%)	(59%)	(7%)
Year high		100.00	73.00	64.50	60.83	134.25	17.35	125.97
Year low		45.50	57.88	40.00	44.38	111.75	6.45	99.79

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.

Government admits Energy Bill will hit consumers in their wallets

The government has conceded that proposals to secure the future of the UK's energy supply will lead to a short-term rise in the costs faced by consumers.

The draft *Energy Bill*—which encompasses Electricity Market Reform (EMR) proposals—will attempt to stimulate over £100bn of private investment in low-carbon electricity.

The introduction of new low-carbon generation incentives in the form of contracts for difference feed-in tariffs (CfD FiTs), capacity support in the form of a capacity market, and an emissions performance standard of 450g/kWh are the three mechanisms to drive the proposed policy forward.

The government has acknowledged the measures will add to consumers' energy bills in the short term, but it claimed energy bills would rise with or without reforms largely because of increases in the price of fossil fuels.

A perfect FiT?

CfD FiTs will replace existing subsidies for large-scale renewables projects—provided under the Renewables Obligation—from 2017. They will provide a financial return for each unit of low-carbon energy generated over the lifetime of new low-carbon plants in a bid to overcome the high capital cost of building them. The rate paid to each project will vary by technology type—with more mature technologies receiving a lower subsidy—as well as differing over time as the cost of building such plants falls.

The government has decided National Grid, as the electricity system operator, is best placed to administer the new mechanism. But the government has acknowledged there could be some conflicts of interest for the company in its current and future roles. To mitigate this risk, the overall direction of the policy and the setting of tariffs will remain with ministers. The first contract and the proposed incentive payments are expected to be published next year.

Gas on stand-by to provide back-up for renewables

A new capacity market has been mooted as a way of ensuring there is a reliable and flexible capacity to help balance intermittent production from renewable energy plants. The government's plan involves paying holders of back-up capacity, mainly gas-fired power plants, to switch on or off at short notice on days of low wind..

The government is likely to consult further on the proposals next year and have the market in place by 2014. But it has made clear this mechanism will only be called upon if necessary.

Emissions standard set to hit coal

The Bill also includes the introduction of an emissions performance standard at 450g/kWh, effectively banning the construction of new coal-fired power plants without carbon capture and storage capabilities.

To further incentivise investment in lower carbon generation, a carbon floor price, which will start at £16/tCO2 on 1 April next year, is to be instigated separately through the Treasury.

The *Energy Bill* will go through pre-legislative scrutiny from the energy and climate change select committee of MPs before being formally introduced into parliament` in the autumn of this year.

The government estimates that with its electricity market reforms the increase in domestic energy bills over the period to 2030 will be £100. But this figure would be doubled without the new mechanisms.

Government

Big business hits out at lack of urgency on carbon reporting

A group of Britain's largest businesses have called on the government to introduce mandatory carbon emissions reporting for larger organisations "as soon as possible".

In a letter to deputy prime minister Nick Clegg on 8 May, the electricity system operator National Grid and a raft of other household names claimed the introduction of such rules would lead to "reduced energy costs, increased transparency and a greater understanding of material climate risks and opportunities".

The letter, signed by retail giants Asda and M&S, goes on to state how three quarters of respondents polled in a recent survey commissioned by the Aldersgate Group want to see mandatory reporting rules introduced. It also suggested the decision on mandatory reporting is "a litmus test" for the government's wider commitment to the low-carbon economy; it will also test its pledge to be the "greenest ever".

A ministerial decision on the introduction of such a scheme was expected earlier this year. But in April the government announced the deadline for its introduction had been missed because more time was needed to consider it. The group said it was "extremely disappointing" that no decision had been made despite a four-year evidence gathering process. "Businesses are seeking greater clarity from government and it is essential that a decision be taken swiftly," it said.

The Aldersgate Group survey, conducted by Populus with a sample of more than 2,000 people, also found 83% of public sector employees and 76% of private sector employees felt large businesses should be required to report their carbon emissions.

Although carbon reporting will have some cost implications for businesses, most stakeholders have argued that increased visibility is worth the price.

Meanwhile, research from the Institute of Environmental Management and Assessment, which conducted a further poll of approximately 1,000 businesses, revealed 90% were in favour of mandatory carbon reporting.

Aldersgate Group

Further gloom for developers as more solar FiT cuts announced

Rates paid to businesses and householders for producing electricity using solar photovoltaic (PV) technologies under the existing feed-in-tariff (FiT) scheme will be cut again later this year.

Under the FiT scheme established in April 2010 the property owner is paid for supplying their own electricity and selling any excess back to the grid. A rate of 43.3p/kWh was available in the early days of the scheme for schemes of up to 4kW, but this was reduced to 21p/kWh in April this year. Electricity suppliers then recover the monies they have paid from all customers.

The government said the new tariffs should give a return on investment of about 6%. Manufacturers and developers now need to see a period of stability under the FiT regime.

The government has now announced that from 1 August the tariff for small-scale installations will be 16p/kWh. This figure is also set to drop by 3%–28% after each three-month review period—unless the market "slows down". If the market loses pace, cuts could be frozen for up to six months. But to better reflect the value of the electricity, the rate for power exported to the grid will be increased from 3.2p/kWh to 4.5p/kWh.

Other changes include an increase in the multi-installation tariff to 90% of the standard tariff and a reduction in the scheme lifetime from 25 to 20 years for new installations.

Government

Cameron seeks global help to shelter UK from "volatile energy prices"

Prime ministers David Cameron has said the UK must work with its global partners to confront the energy issues jeopardising economic growth. Speaking on 17 May, Cameron called for international recognition of "the risks to the [economic] recovery from rising and volatile energy prices". To face these challenges he said it is vital countries "work together" to secure energy supplies and added international collaboration is vital to "keep Britain safe from the storm".

No 10

Energy costs and reliability remain key business concerns

The cost of energy is one of the two most important infrastructure issues faced by small businesses in the UK, according to new research.

A survey by the Forum of Private Business reported on 10 May that 80% of their members who responded on "infrastructure for growth" believed energy costs were "important" or "very important". The survey also reported 75% of respondents believed reliability of energy supply was also a key issue. Telecommunications was joint top of the list of concerns, while local issues such as banking services and roads also featured prominently.

The Forum called on the government to build a "joined-up system where projects on transport and communication work in harmony with proactive policies on energy, tax and red tape to boost business […] and put the economy back on track."

Forum of Private Business

Green Deal hits the road to recruit SMEs

Small- and medium-sized businesses (SMEs) are to be shown the benefits of getting involved in the multi-billion pound Green Deal energy efficiency scheme at a series of government-run briefings. They will be held in 11 UK cities throughout June and July as attempts to secure more SMEs as Green Deal providers are ramped up ahead of the scheme's launch in October.

This announcement follows a report, commissioned by the Green Deal Skills Alliance, which estimated SMEs could boost turnover by up to 20% by subcontracting for larger companies under the Green Deal.

Government Green Deal Skills Alliance

Low-carbon innovation given major financial backing

A £35mn Energy Entrepreneurs Fund to support small- and medium-sized businesses (SMEs) develop and demonstrate low-carbon technologies has been unveiled by global decision-makers.

The financial backing was unveiled during April's Clean Energy Ministerial Summit in London, where ministers from around the world sought to find solutions to accelerate the progress of global clean energy policy. Alongside the new fund for SMEs, a raft of other policy announcements were made. These included initiatives to boost the take-up of biomass for energy production, and support for advanced heat storage technologies and small-scale energy-from-waste.

Clean Energy Ministerial

Government seeks to lift the smog of emissions bureaucracy

Small emitters and hospitals will be given the option to opt-out of Phase III of the EU Emissions Trading Scheme (EU ETS) from 2013. The announcement of 25 May came as the government seeks to advance its pledge to cut regulation obstructing businesses.

To be eligible for the "lighter touch" scheme, organisations must have verified annual emissions of less than 25,000 tCO_2e from 2008 to date. The government has estimated these organisations account for just 1% of annual UK EU ETS emissions, but they can see administration costs of £1/tCO_2—compared to £0.04/tCO_2 for larger emitters. Interested organisations have until 18 July to apply for the exemption, which will take effect from January 2013.

Government