# Energy Element / November 2014

CATALYST ENERGY SOLUTIONS

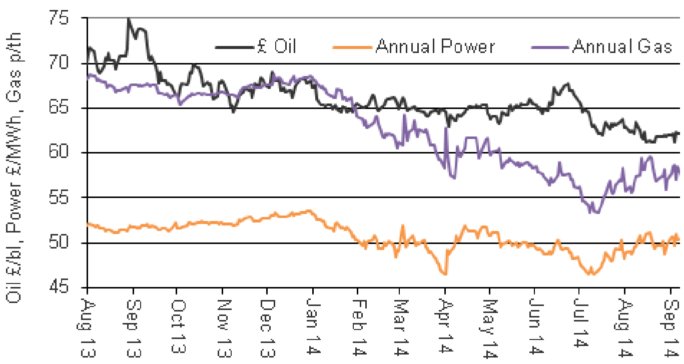
In this issue…



## Oil prices tumble to four-year lows

Oil prices fell to their lowest level in four years on concerns that global supply is outstripping demand. These reductions in oil had a knock on effect on gas and power prices in the UK and were compounded by a recent report by the International Energy Agency claiming that global oil demand is set to increase more slowly than previously estimated.

**Crude oil and annual wholesale gas and power prices**



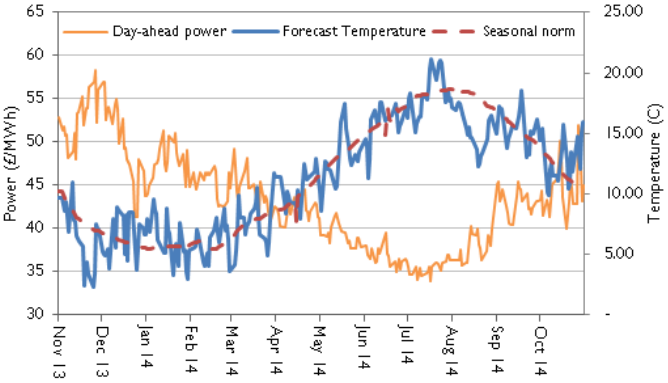

### Long-term contract follow oil reductions

Reductions in oil and other commodities fed into gas and power prices.

Long-term gas contracts fell in October. Summer 15 gas dropped 4.2% to average 53.1p/th and the contract ended trading 16% below levels seen at the start of 2014. Long-term power prices also dropped in October, with the summer 15 power contract losing 2.3% to average £48.5/MWh.

A fire at Didcot B power station, nuclear outages and rising demand pushed up short-term gas and power prices. However, increases were limited by the imminent return of some capacity and high wind speeds. Day-ahead gas rose 4.1% over the month to average 50.5p/th. The contract rose to a five-month high of 52.7p/th on 29 October. Day-ahead power prices continued to rise in October, gaining 4.3% over the month to average £45.0/MWh. The contract rose to a 12-month high of £52.0MWh on 28 October.

**Spot power prices and temperatures**



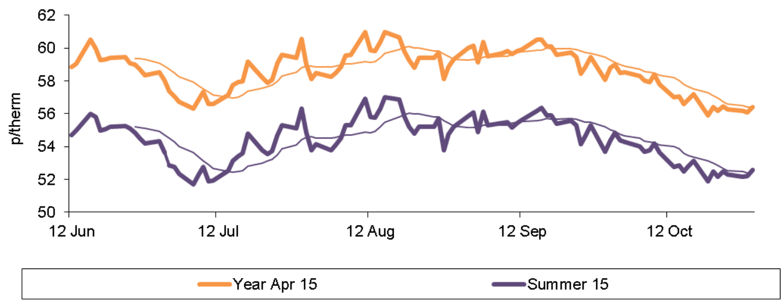

### The month ahead: worsening UK power margins but secure gas supplies

In its 2014-15 *Winter Outlook* report, which was released on 28 October, National Grid stated that electricity margins are set to decrease this winter, with the average cold spell margin expected to be 4.1% – the narrowest margin seen since 2006-07. The industry consensus is that power supplies will meet demand this winter, but that the cost of electricity may rise as a result of lower supplies than in recent years.

Gas supplies, on the other hand, are in a strong position this winter. National Grid expects supplies, storage and network capacity to be well in excess of demand. Russia's agreement to resume gas supplies to Ukraine will also help ensure the EU (and therefore the UK) has secure supplies this winter. This followed news that news that the Rough gas storage facility in the North Sea is full to record levels. Plentiful supplies normally result in stable prices, but temperatures will play an important role in the season ahead.

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.

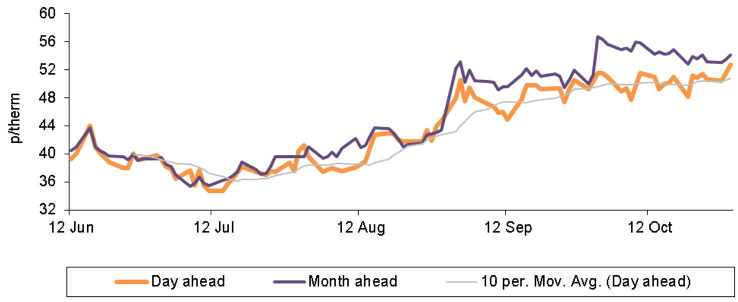
## Annual gas prices




Long-term gas prices fell October, as Russia and Ukraine reached a deal on gas debt and oil prices tumbled.

Summer 15 gas dropped 4.2% to average 53.1p/th. The annual April contract fell 4.1% to average 57.2p/th.

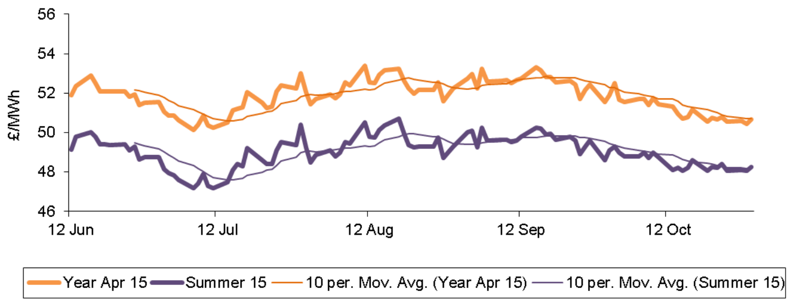
## Spot gas prices




In contrast to long-term trends, the spot gas market climbed higher in October, with day-ahead gas rising 4.3% to average 50.5p/th. The increase in gas prices came despite mild temperatures and record high storage levels.

The month-ahead contract followed spot trends, gaining 6.4% to average 54.6p/th. Rises were dampened however by the high supply picture for the upcoming winter.

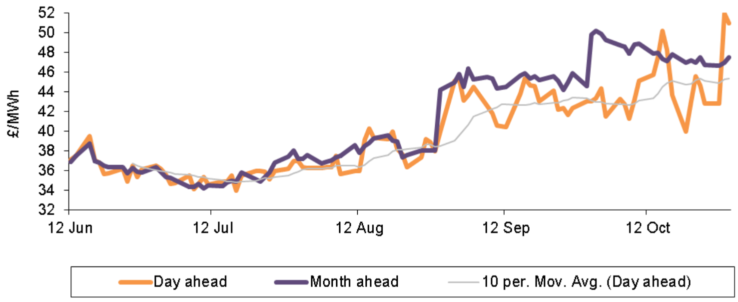
## Annual power prices




Lower coal, gas and oil prices all weighed on long-term power contracts in October and the imminent return of two-nuclear power stations helped alleviate some security of supply concerns.

Summer 2015 power dropped 2.3% month-on-month to £48.5/MWh. Annual April 2015 was down 2.8% to £51.1/MWh.

## Spot power prices




Spot power prices followed the trend in gas contracts this month; however, strong wind speeds helped limit rises.

Month-on-month, day-ahead power averaged 4.3% higher in September at £45.0/MWh. The contract rose to £52.0/MWh on 28 October.

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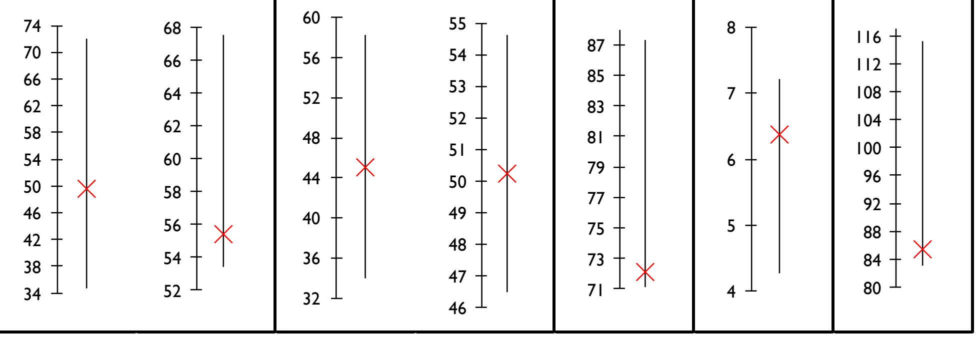
### Key market indicators: 31/10/2014

| | | Gas (p/th) | | Electricity (£/MWh) | | Coal | Carbon | Brent crude |
|---|---|---|---|---|---|---|---|---|
| | | Day-ahead | Year-ahead | Day-ahead | Year-ahead | ($/t) | (€/t) | ($/bl) |
| July | 31 Oct 14 | 49.50 | 55.44 | 45.00 | 50.25 | 72.10 | 6.37 | 85.33 |
| June | 2 Oct 14 | 51.55 | 58.47 | 44.35 | 51.65 | 74.50 | 5.75 | 92.90 |
| Last year | 1 Nov 13 | 66.50 | 64.38 | 52.80 | 54.80 | 82.55 | 4.85 | 109.21 |
| Year-on-year % change | | (26%) | (14%) | (15%) | (8%) | (13%) | 31% | (22%) |
| Year high | | 71.95 | 67.53 | 58.30 | 54.63 | 87.30 | 7.22 | 115.20 |
| Year low | | 34.70 | 53.38 | 34.00 | 46.48 | 71.10 | 4.27 | 83.00 |

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.

### Disclaimer

# Energy in spotlight during conference season

The UK's three major political parties have used their autumn conferences to set out their visions for the future of the energy sector.

### Changing the rules

Speaking at the Labour Party conference on 23 September, leader Ed Miliband said that a Labour government would ensure Britain maintained its position as "a world leader in the green economy" as a means to unlock business investment. He detailed plans to set a decarbonisation target for the power sector, to give the Green Investment Bank full borrowing powers, and to make energy efficiency a national priority.

In her speech on 22 September, shadow energy and climate change secretary Caroline Flint reaffirmed Labour's commitment to introducing a 20-month energy price freeze if elected next year. Labour, she said, would use those 20 months to "change the rules of the game", creating a new regulator "with a bite as good as its bark", and with the power to ensure that reductions in wholesale prices were passed onto consumers.

### Security focus

Speaking at the Conservative Party conference on 30 September, energy minister Matt Hancock said that ensuring energy security should be part of "any vision for a better Britain", and that the government was making progress to this end "in a dangerous and uncertain world". "We've seen record investment in energy in this Parliament, but there's more to do. We must unlock the shale wealth beneath our feet. We must invest in new nuclear [power]. And we must ensure that the renewables we support are the best value for bill payers and taxpayers alike", Hancock said.

Chancellor George Osborne reinforced Hancock's emphasis on the need to ensure security of supply, while prime minister David Cameron stressed that a Tory government would ensure Britain remained a world-leader in efforts to tackle climate change.

### A green vision

Speaking at the Liberal Democrat conference on 7 October, energy and climate change secretary Ed Davey noted the "dramatic changes" made in the energy sector by the coalition; but he said a Liberal Democrat government would take this further and deliver the "green power revolution" that Britain needed.

Davey argued that the "real fossil fuel enemy" was coal; he re-affirmed the Liberal Democrats' pledge that, if in government after the next election, it would legislate to ban coal-fired power generation without carbon capture and storage by 2025. He also noted that, while shale gas was not a "magic bullet", the resource was needed to act "as a bridge to a zero fossil fuel future, at least for the next two or three decades". Davey argued that it would be preferable to exploit Britain's domestic gas reserves than to import the fuel from Russia or the Middle East.

Deputy prime minister Nick Clegg used his conference speech to note that a Liberal Democrat government would implement a "budget that is balanced overall, but allows us to invest in our creaking infrastructure too". A sustainable environment remains at the "heart of our vision" and will ensure the environment is safeguarded for future generations, he concluded.

**The sector's current political prominence is hardly surprising in light of sharp household price increases over recent years, and parties now see their ability to deliver the low-carbon transition affordably as a key issue for consumers.**

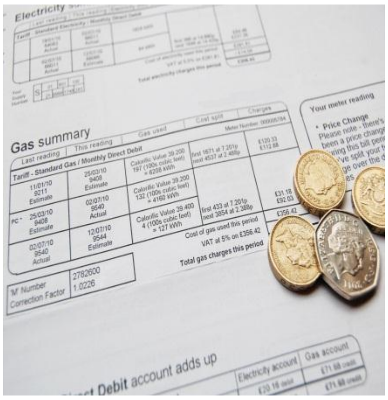
Labour Conservatives Liberal Democrats

## Non-domestic tariffs should be published: FSB

The Federation of Small Businesses (FSB) has called on the next government to implement fundamental reforms to the energy market.

### Cost barrier for small businesses

In its *Business Manifesto for the 2015-20 Government*, published on 29 September, the organisation said that small firms were struggling to engage effectively in the energy sector owing to their "limited purchasing power and expertise". It suggested that around a third of small businesses regarded the cost of energy as a barrier to the growth and success of their business. It said the next government should treat small businesses in a similar way to domestic consumers, affording them similar status in the energy markets.




### Better information

Among other measures, the lobbyist recommended that the future government improved the provision of customer-focused information to small businesses in energy, banking, water and telecoms. Noting that four in five FSB members agreed that published tariffs would benefit their business, the organisation urged the government to require energy suppliers to publish non-domestic gas and electricity tariffs.

The report also called for a complete ban on automatic rollover contracts, and said the future government should support Ofgem's proposals to improve the market for non-domestic consumers, including shortening the maximum termination notice period to 30 days.

### Increasing trust

The FSB acknowledged that energy brokers played an important role in helping businesses get good deals from suppliers. But it called on the next government to regulate intermediaries and to ensure that suppliers only worked with brokers that had signed up to a code of practice.

The manifesto also said that the Carbon Price Floor should be scrapped.

FSB

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## Hinkley Point C given state aid clearance

The European Commission has approved the government's support package for the proposed Hinkley Point C nuclear power plant.

Last October the government announced that the developer, EDF, would benefit from a 35-year contract for difference (CfD), providing it with a fixed price of £92.50/MWh for electricity generated by the Somerset plant. If wholesale prices rise above an agreed strike price, the profits will be returned to consumers, but if prices fall below this price, the generator will receive a top-up payment. In addition the company will be awarded a UK Infrastructure Guarantee, which will help it to unlock finance prior to operation.

The European Commission ruled, on 8 October, that the CfD and the Infrastructure Guarantee constituted a proportionate way for the UK to meet its low-carbon objectives. Energy and climate change secretary Ed Davey said that the decision demonstrated the Commission's agreement that the contract represented a "good deal for consumers".

But continuing cost concerns saw the National Audit Office (NAO) confirm on 16 October that it would investigate the agreement. The office said that its work would cover the government's commercial approach to securing the deal and the proposed terms of the contract, so that the NAO could report to Parliament on value for money and the risks that the government would need to manage.

European Commission

# Government welcomes "huge" capacity market interest

Over 60GW of de-rated capacity has applied to participate in the first capacity market auction, which will be held in December, the government has announced.

### Back-ups

The aim of the capacity market is to ensure that there is sufficient electricity generation capacity available at all times to meet projected levels of demand. Recognising that the market may not make this capacity available without some form of incentive, the government is to introduce a market to make payments to certain power stations for being available to generate as and when required. Large energy consumers could also win contracts to reduce their demand at times of system stress.

The government has said that it plans to contract for 53.3GW of peak generating capacity for delivery in winter 2018-19.

### On target

On 3 October the government said that 513 separate applications had been received from the industry to take part in the scheme, and that over 62GW had been accepted as eligible to participate. Those successful at pre-qualification included approximately 9GW of new capacity – 7GW of which came from eight large gas-fired power stations.

Welcoming the "huge" levels of interest, energy and climate change secretary Ed Davey said the government had responded to "an energy crunch caused by a legacy of underinvestment". The interest shown by the industry "shows that we'll be able to deliver the capacity we need, and get a good deal for bill payers in the process", Davey added.

The successful applicants will now compete in an auction, set to be held in December, which will allocate 95% of the 53.3GW required from 2018-19. The rest is set to be auctioned in 2017.

**Based on the prequalification, the government's target to procure 53.3GW of capacity should easily be met.**

Government

# Government must cut smart meter costs: FSB

The Federation of Small Businesses (FSB) has called for the government to "play fair" when rolling out smart energy meters to non-domestic customers. The FSB claimed many businesses were confused where they fit into the roll-out and on what guidance was available to them. It also urged the government to take immediate action to reassess the costs of the roll-out and the impact that these could have on business energy costs.

Separately, consumer group Which? has written to the government calling for new measures to lower the cost of the smart meter roll-out. In a letter to energy and climate secretary Ed Davey, dated 7 October, the organisation acknowledged that the technology would give consumers more control over their energy use, but added that it was "imperative" for costs to be reduced "wherever possible".

Specifically, the government was urged to explore: centralised procurement of meters; a coordinated approach to the installation of communications infrastructure in multi-occupancy buildings; and early guidance on all "reasonable steps" that suppliers need to take to install the meters by 2020.

Which? Businessgreen

## Businesses call for “robust” 2030 climate targets

The Aldersgate Group, EDF Energy, SSE, Tesco, Kingfisher and Shell are among a group of businesses urging EU leaders to set out a clear vision for the future of the energy sector.

In an open letter, published on 6 October, the Prince of Wales’ Corporate Leaders Group (PWCLG), with the support of 57 companies, raised concerns about the costs, risks and impacts associated with delayed action on climate change. It called on policy-makers to make “timely decisions” about future energy and climate policies. In particular the signatories urged policy-makers to urgently agree a robust 2030 energy and climate policy framework and energy security strategy that can deliver a global climate change agreement in 2015. The businesses called for “an early structural reform” of the EU Emissions Trading Scheme (EU ETS) as a means to boost carbon prices – encouraging low-carbon investment.

Separately the European Council announced on 24 October that it had agreed on an energy and climate framework for the EU through to 2030. The agreement incorporates a 40% emissions reduction target, which will be delivered through a 43% emissions cut in sectors covered by the EU ETS, and a 30% reduction for sectors outside it. The Council further confirmed a 27% renewables target and an indicative 27% target for improving energy efficiency.

PWCLG European Council

## Energy policy must support a balanced economy, say manufacturers

A rapid rise in electricity costs could undermine Britain’s ambitions for a better-balanced economy, manufacturers’ organisation EEF has claimed.

In its *Manufacturing: Powering the Economy: An Agenda for Government to 2020* report, published on 13 October, the organisation predicted a 50% increase in electricity costs by 2020, which it said would damage investment, reduce business margins and damage the competitiveness of UK companies, “putting the brakes on growth and leaving our economy stuck in the slow lane”. The report suggested that 73% of manufacturers felt an increase of this magnitude would have a notable impact on their margins, and that 34% said they would be forced to cut spending in other areas of their businesses. 25% in the sector said they would consider investing in facilities overseas.

To ensure British businesses remain competitive, EEF called on the government to implement a fresh approach to energy efficiency and to review the cost of moving to a low-carbon economy. It welcomed the government’s pledge to compensate selected industries for the costs of certain policies, and said it was “vital” that policy-makers help unlock energy efficiency opportunities in a manner that “minimises or neutralises any negative competitive effects”.

EEF

## Government opts against changes to CRC report

The government has confirmed that it will not progress its plans to make changes to the Annual Report Publication (ARP) of the Carbon Reduction Commitment (CRC) energy efficiency scheme. Earlier this year the government set out plans to publish additional data sets to give public recognition for investment in onsite renewables via the CRC, along with a series of other changes. But, in a response issued on 22 September, the government said that although the changes were small, respondents had expressed a clear preference for stability and to give recently implemented reforms to the CRC a chance to “bed down”.

Government

## EU could halve gas imports by 2030

Stronger investment in renewable energy and energy efficiency could see the EU significantly reduce its natural gas imports by the end of the next decade, according to consultant Ecofys. Issued on 20 October, a study by the analyst suggested that the development of cost-effective measures could see gas consumption in buildings and industry reduced by 58% and 20% respectively by 2030. Overall, it argued the EU could reduce its carbon emissions by 49% by 2030 – significantly higher than the 40% target currently being proposed.

Ecofys