

## In this issue...

- 1 Winter 16 contracts at nine-month high
- 2 Wholesale market snapshot
- 3 Key market indicators
- 4 New prime minister links business and energy departments
- 5 UK set to miss renewables target
- 6 Government delays decision on new nuclear project

## Winter 16 contracts at nine-month high

Gains in commodity markets created a bullish trend in the GB energy market in July, with all gas and power contracts experiencing gains.

Seasonal gas prices gained 9.0% on average, despite a fall in oil prices. Winter 16 gas experienced the largest increase (of 10.2%) to average 44.7p/th, a new nine-month high. Summer 17 gas was up by 7.8% to 40.4p/th.

Centrica announced it had extended the closure of its Rough gas storage site, the UK's largest, until spring 2017 following the discovery of an issue with one of its wells. This has caused concerns around storage supplies for the coming winter, and contributed to the large rises in the winter 16 contract. Day-ahead gas moved 0.5% higher to average 34.5p/th.

Seasonal baseload power contracts on average climbed 6.7% in July, following their gas counterparts higher. Winter 16 power lifted 7.7% to £47.2/MWh, peaking at £48.3/MWh on 18 July. Day-ahead power also followed its gas counterpart, up 2.6% to £38.2/MWh, the highest average in nine months.

## Oil prices reach a three-month low, coal prices at 16-month high

Brent crude oil prices lost 5.3% to average \$47.2/bl in July. Prices have fallen from their near eight-month high of \$52.2/bl in early June, driven by re-emerging concerns of

oversupply in the market.

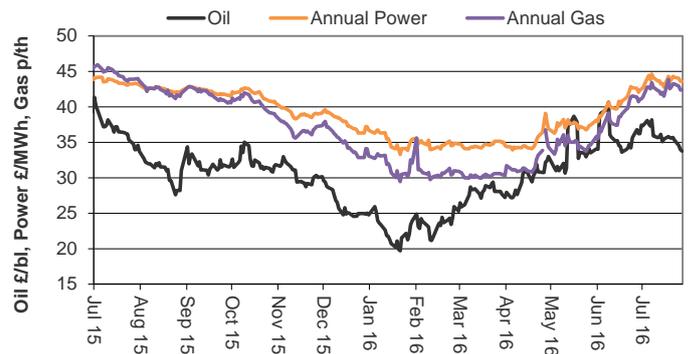
Prices dropped to their lowest point in three months on 27 July, at \$44.28/bl. At the start of the month, prices fell amid worries about an economic slowdown following Britain's vote to exit the EU. They were pushed down further as US producers increased the number of active rigs to the highest since April, while Canadian supplies rose and Asia weakened economically.

Mid-way through the month the IEA released its *Oil Market Report* for July. It showed that global oil supplies rose by 0.6mb/d in June, to 96mb/d, after outages curbed OPEC and non-OPEC supplies in May.

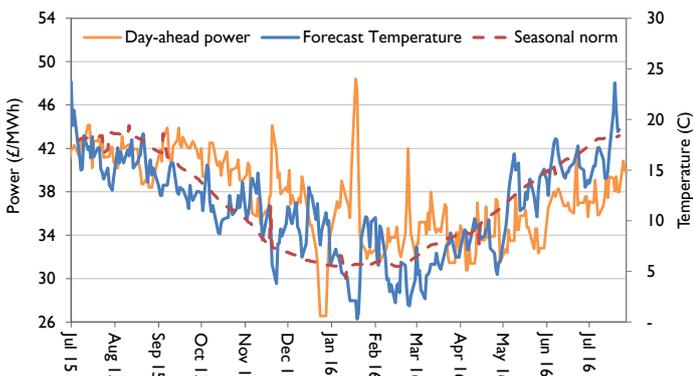
API 2 coal rose 9.1% to average \$58.8/t. On 18 July prices reached a 16-month high of \$60.5/t. Recent gains can be largely attributed to reduced Chinese production, which has fallen 8.4% year-on-year over the January-May 2016 period.

EU ETS carbon dropped 17.4% to average €4.7/t. According to Thomson Reuters, carbon prices have fallen almost 20% since the UK voted to leave the EU on 23 June. Moody's expects EU ETS prices to remain "broadly flat" in the five years

## Crude oil and annual wholesale gas and power prices



## Spot power prices and temperatures



to 2021, which would mean a sustained period of dampened EU ETS costs, and therefore reduce the incentive to switch to cleaner fuels.

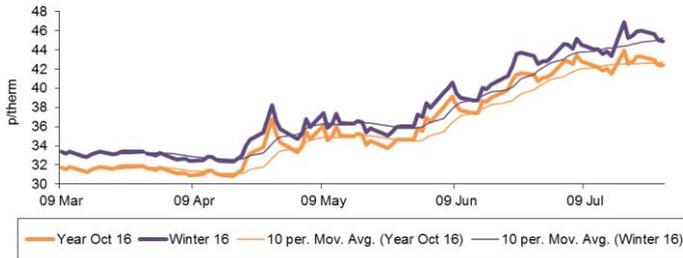
## The month ahead: Further rebound expected

Commodity prices have rebounded from lows earlier this year and this trend is expected to continue in August.

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## Annual gas prices

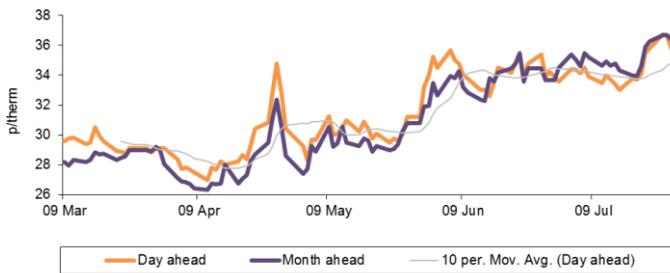


All seasonal gas prices increased in July. The annual October 16 gas contract rose 9.0% to 42.6p/th.

Winter 16 gas experienced the largest increase of 10.2% to average 44.7p/th, a nine-month high. Summer 17 gas was up 7.8% to 40.4p/th.

Centrica announced that it had extended the closure of its Rough gas storage site, the UK's largest, until spring 2017 following the discovery of an issue with one of its wells. This has caused concerns around storage supplies for the coming winter, and has caused large rises in the contract.

## Spot gas prices

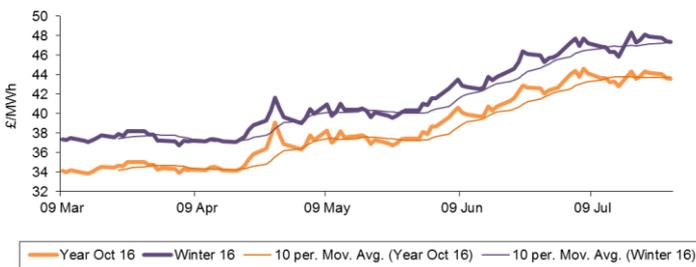


Spot gas prices also rose in July, with day-ahead gas up 0.5% to 34.5p/th.

The month-ahead contract gained 2.7% to average 35.2p/th.

Gas-fired generation provided 45.8% of GB's electricity mix during the month, while coal only produced 4.3%, as cheaper gas prices have made it the dominant fuel.

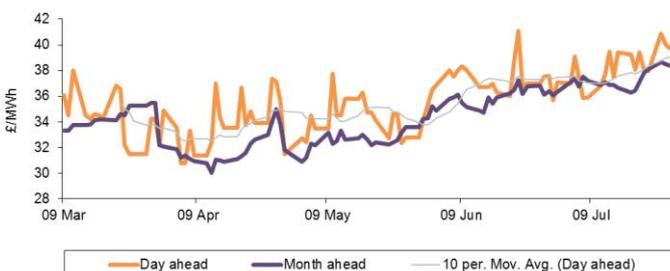
## Annual power prices



The annual October 16 baseload power contract improved 7.3% to average £43.8/MWh, following the gas market higher.

Winter 16 power gained 7.7% to average £47.2/MWh. The contract reached a high of £48.3/MWh on 18 July, the highest price since March 2015. The contract followed its gas counterpart upwards, which was supported by news that the Rough gas storage facility could be closed until spring next year. Summer 17 increased 7.0% to £40.4/MWh.

## Spot power prices



Spot power prices moved 2.6% higher to average £38.2/MWh, the highest average in nine months. The contract followed its gas counterpart higher.

The month-ahead contract grew 4.4% to average £37.3/MWh during July.



# Energy Element / August 2016

## Key market indicators: 27/07/2016

	Gas (p/th)		Electricity (£/MWh)		Coal	Carbon	Brent crude
	Day-ahead	Year-ahead	Day-ahead	Year-ahead	(\$/t)	(€/t)	(\$/bl)
This month 27 Jul 16	35.80	42.39	39.75	43.60	60.20	4.54	44.28
Last month 30 Jun 16	33.90	41.13	35.70	42.53	55.25	4.55	50.24
Last year 27 Jul 15	42.30	44.57	41.25	43.40	56.90	8.04	54.17
Year-on-year % change	(15%)	(5%)	(4%)	0%	6%	(44%)	(18%)
Year high	45.00	48.38	48.40	45.65	60.50	8.64	66.01
Year low	27.00	29.88	26.56	32.84	36.55	4.69	27.83

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.

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## New prime minister merges business and energy departments

Theresa May's new government has implemented major reforms to the way in which it oversees the setting and delivery of energy policy in the UK.

The day after becoming prime minister on 14 July, May confirmed that the Department of Energy and Climate Change (DECC) would be abolished.

The department had been established in 2008 under the Labour government, and has since been accountable for shaping the UK's response to the so-called energy "trilemma": ensuring security of supply, keeping bills low, and lowering emissions.



### New department

In DECC's place, May has established the Department of Business, Energy and Industrial Strategy (BEIS). This will further take on some of the responsibilities that formerly belonged to the Department of Business, Innovation and Skills, which has also been abolished.

In an explanatory note, the government said that the changes would better position the UK to deliver the new investment and innovation needed to support the UK's future energy policy. It explained that one of the main challenges in combatting climate change was to reduce emissions without jeopardising economic growth, and that the merger would help to balance these priorities.

The note added: "Bringing together energy policy with industrial strategy will be beneficial to shaping a competitive business environment for energy intensive industries, including the UK steel sector. The new department will have a strong focus on the needs of customers, both business and domestic."

### Ministerial re-shuffle

BEIS will be led by Greg Clark, who previously served as communities and local government secretary. Clark also served as shadow energy and climate change secretary in 2008, and strongly supported policies that set in law the UK's long-term environmental goals.

A number of ministers will support Clark at the department, including Nick Hurd, who has similarly expressed strong support for the low-carbon transition. Hurd is a member of the Conservative Environment Network, which seeks market-based solutions to environmental challenges. Other ministers at the department include Jo Johnson, Margot James, Jesse Norman, and Baroness Neville-Rolfe.

### Industry reaction

The energy industry's reaction to the changes was mixed, with many environmental groups expressing concern about the abolition of a department explicitly committed to addressing climate change. The Institutional Investors Group on Climate Change said that investors would be seeking early assurance that the changes did not represent a downgrading of the UK's commitment to the low-carbon transition.

However, stakeholders responded positively to the appointment of Greg Clark, with the Renewable Energy Association saying: "He previously showed real vision as the shadow energy secretary and we look forward to working with him once again in order to get things moving on the deployment of new renewable energy infrastructure."

**The appointment of an experienced minister to head up the new department has done much to settle initial nerves about the departmental reforms.**

### Government



## UK set to miss renewables target

New analysis by the energy system operator has suggested that the UK will fall short of its target for deploying renewable energy technologies by the end of the decade.



The European Union (EU) has set the UK a binding target of delivering 15% of its energy from renewable sources by 2020. To meet this overarching goal, the UK has set itself a series of sub-targets: it is aiming for 30% of electricity to come from renewables sources, 12% of heat, and 10% of transport. However, in its annual *Future Energy Scenarios* (FES) study, issued on 2 July, National Grid suggested that the UK would fail to meet its 2020 target.

### Slow progress

The aim of the FES report is to model plausible scenarios for the UK's energy system over the next few decades, and to evaluate the impact of these across the generation, heat and transport sectors. Even the report's most optimistic scenario for decarbonisation - "Gone Green" - showed the UK only reaching its 15% target in 2022 - two years after the deadline set by the EU. Meanwhile, the report's "No Progression" scenario, which focuses on affordability over decarbonisation, sees the target hit in 2029.

Concerns about the pace of progress on deploying renewables relate primarily to the heat and transport sectors. For example, the report suggested that, to meet the sub-target for heat, renewables generation would need to increase by 60TWh on 2016 levels – whereas over the past four years it has increased by less than 10TWh. National Grid concluded that the pace of development would therefore need to increase "significantly".

The impact of the UK's vote to leave the EU on the nation's renewable energy goals remains unclear, and will be determined through negotiations on the future relationship between the two.

### Secure supplies

In all of the report's scenarios, the anticipated closure of nuclear and coal-powered plants over the coming years would make necessary the development of new sources of electricity generation. Security of supply would, it said, be maintained through an increasingly diverse combination of technologies: small-scale thermal generation, new low-carbon projects, and the importing of power from abroad through interconnectors. However, gas-fired power generation was expected to remain the "backbone" of the UK's electricity supply.

National Grid was optimistic about the potential for the roll-out of new energy technologies in the UK. It said up to 18GW of energy storage, which is seen as crucial to supporting the growing level of intermittent renewables on the system, could be deployed by 2040.

**The analysis will be concerning to the government; in or out of the EU, the UK has ambitious decarbonisation objectives, and a clear path towards meeting them will need to be mapped out over the coming year.**

National Grid

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## Businesses can help ease supply concerns by varying demand, report says

Manufacturing sites, hospitals and retail stores could provide the equivalent electricity supply of six new power stations and help to address concerns about the UK's power supply, a report has said.

The report, issued on 19 July by the Association for Decentralised Energy (ADE), said that up to 16% of the UK's peak electricity requirement could be met through businesses flexing their demand for power.

Growing doubts have been expressed about the UK's ability to "keep the lights on", as old power stations shut down and less reliable renewables projects come online. But one part of the solution, ADE said, was to incentivise businesses to better manage their energy use in return for payments – known as "demand-side response" (DSR).

The report's analysis suggested that, by unlocking the potential of the DSR sector, UK consumers could save up to £600mn by 2020 and £2.3bn by 2035.

ADE



### Government delays decision on new nuclear project

The government has announced that it will review EDF's plans for a new nuclear power station at Hinkley Point C in Somerset before finally signing off on the project.

On 28 July, EDF announced a Final Investment Decision (FID) on the plant, after a string of delays. However, within hours, business, energy and industrial strategy secretary Greg Clark issued a statement, saying: "The UK needs a reliable and secure energy supply and the government believes that nuclear energy is an important part of the mix. The government will now consider carefully all the component parts of this project and make its decision in the early autumn."

#### Project preparations

The then coalition government initially granted planning approval for Hinkley Point in 2013, having committed to supporting the development of a new fleet of nuclear power stations in Britain. Later that year, an agreement was reached for the government to provide subsidies for the project through its new low-carbon support mechanism, known as contracts for difference (CfD).

Specifically, the contract confirmed that EDF would receive £92.50/ MWh for electricity produced by the plant's reactors over a 35-year period. These subsidies are ultimately recovered through consumers' energy bills.

However, over the next year-and-a-half, EDF deferred a Final Investment Decision on the plant, as it waited for the European Commission to approve the CfD, and so that the company could consult with unions. It had expected, following the FID announcement, to sign final contracts with the government and key suppliers for the plant, but this will now be delayed while the government conducts its review.

#### Cost concerns

The government's decision to pause before approving Hinkley has been widely welcomed, as many analysts have raised concerns over the past couple of years about the cost-effectiveness of the project. In a research note published on 29 July, RBC Capital said: "[...] We find it impossible to conclude at this stage that EDF will be able to deliver on time and on budget, and this is likely to remain a considerable risk for many years. As for the overall wisdom of the project for the UK, we question whether such large-scale generation is needed in a rapidly changing and decentralised energy market where the cost of renewables and storage are coming down."

**It does not seem inappropriate for a new government to want to look carefully at a project of this cost and scale before giving final approval. But it does follow a succession of delays from the company itself and therefore adds further doubt about the prospects for the UK's new nuclear power programme.**

EDF



### Coal's share of the electricity mix falls to new low

Electricity generated by coal accounted for just 10% of Britain's electricity mix in the three months through to the end of May, new figures have revealed.

The government's quarterly stats, published on 28 July, indicated that electricity supply from the resource had dropped year-on-year by 66% to a record low of 7TWh. Several coal plants have closed over the past year as market conditions have become more challenging. The government has vowed to remove coal from the system entirely by 2025, and is expected to consult shortly on its plans for delivering on this pledge.

By contrast, gas provided a 48% share of the electricity mix over the same three-month period, with supply up by 68% to 33TWh. The shares of nuclear power and renewables in the generation mix were essentially stable at 22% and 19% respectively.

The figures also revealed that, on a temperature-adjusted basis, fuel consumption in the UK dropped by 1.1%. This is in line with the longer-term trend, and reflects among other factors an improving level of energy efficiency.

Government



### London mayor applies for supply licence

London mayor Sadiq Khan has confirmed that City Hall has taken a significant step towards securing an energy supply licence that could be used to provide clean electricity to public sector organisations.

On 25 July the energy regulator Ofgem announced that Khan could formally advertise his application for a new type of junior electricity supply licence - known as "licence lite". If granted, the Greater London Authority would become the first local authority in the country to hold the licence, which would allow it to buy power from generators and sell it directly to tube stations, offices and other facilities.

Khan hopes that, by providing generators with a better price for their electricity than would otherwise be possible, he can help London to develop more clean power and support around £300mn of investment by 2021.

GLA

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### Solar group warns on increase to business rates

The business rates on commercial rooftop solar installations will increase by between six and eight times from April 2017 unless the government intervenes, an industry group has warned.

The change is coming through a wider re-evaluation of business rates, which takes place every five to seven years. The Valuation Office Agency looks at how assets are valued, the income they generate, and how costs have evolved over that period. But, in a statement on 5 May, the Solar Trade Association said this presented a particular challenge for the solar sector: it said that the rateable value coming into force for the next technology next year bore little relation to the revenue generated by projects, but was instead based on fixed assumptions about the capital cost of installation.

Paul Barwell, chair of the STA said: "This is a huge increase in the running costs of a rooftop solar installation that will affect both existing and new projects. In some cases, it would actually send installations into negative returns: you would be spending more on the system in tax and maintenance than you would be getting back from the sale of the power and the feed-in tariff support."

STA

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### Lack of government incentives stifling business energy efficiency, say consultants

A new survey has found that four fifths of commercial landlords believe that a lack of government incentives represents the biggest barrier to energy efficiency in UK real estate.

The report, unveiled by Tuffin Ferraby Taylor on 8 July, suggested that landlords seeking to invest in energy efficiency were concerned about payback periods, and that three quarters regarded the sector's regulatory framework as too complex at present. More positively, more than nine in 10 (92%) respondents said that attitudes to energy efficiency had improved since the last recession, with a similar proportion (90%) saying that energy efficiency was now a higher priority in their portfolios than it was before 2008.

TFT

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### Ofgem concerned payments to local energy generators distorting competition

The energy regulator has expressed concern about payments being made to small-scale, local power generators, as part of the current arrangements for the British energy networks.

On 29 July Ofgem published an open letter focusing on the payments received by these generators for helping suppliers to reduce the biggest element of the electricity transmission charges they face at peak times. These payments – also known as "embedded benefits" – come in addition to the price that the generators receive for selling their electricity. Large-scale generators connected to the transmission network do not benefit from these payments.

Ofgem believes that these arrangements could be distorting energy market competition and that a level playing field is necessary for all generators. It has invited industry views on whether changes to the current rules should be considered.

Ofgem

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