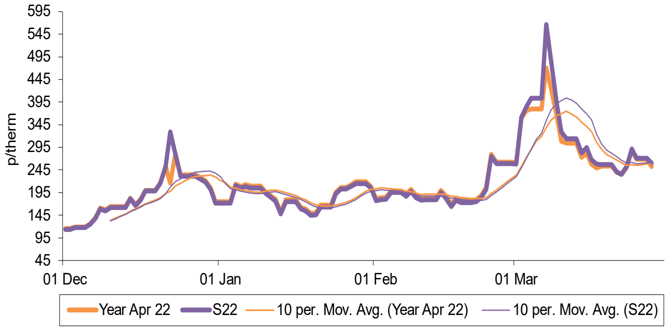
Digital Energy Element

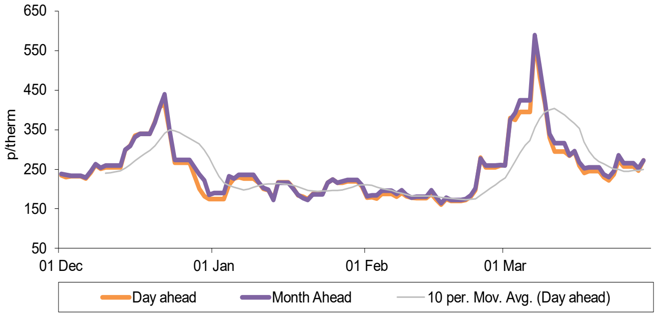
April 2022

The volatility in wholesale energy prices continues

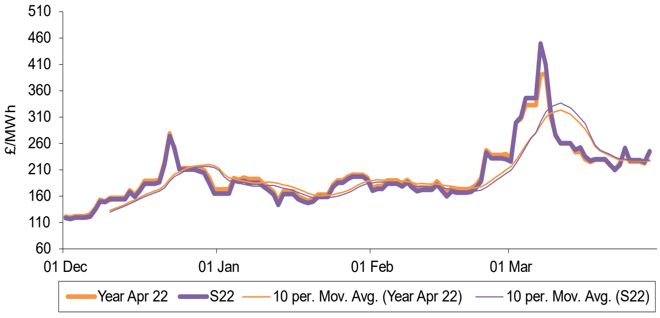
Annual gas prices



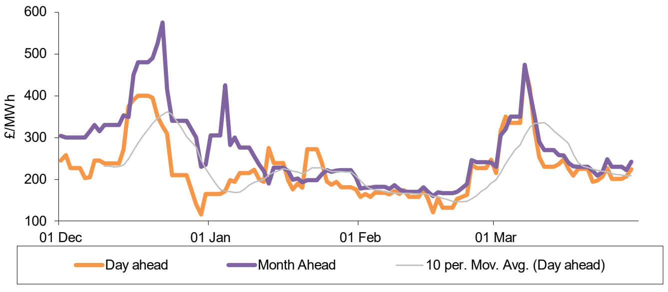
Spot gas prices



Annual power prices



Spot power prices



In March GB gas prices resumed their bullish trends, particularly at the start of the month, bolstered by the speculation and introduction of Russian energy sanctions. Prices did ease from the significantly elevated levels achieved at the start of March, as the month matured, helped by easing immediate supply disruption concerns.

On average, seasonal gas contracts from summer 22 to summer 24 were 40.1% higher in March than in the previous month. Gains were seen particularly in the first week of March boosted by announcements of fresh sanctions imposed on Russian energy imports from the west, although prices retreated by the end of the month.

The volatility in wholesale energy prices remains a prevalent and on-going driver, particularly in GB and Europe, driven by speculation and announcements on western sanctions and Russian response, as well as the tight gas supply landscape prior to conflict in Ukraine. Threats of economic and energy related sanctions ramped up future gas supply concerns for forward delivery, evidenced in the sharp rise in the summer 22 gas contract, which lifted ~63% higher (318.06p/th) in March.

There were some record highs within GB gas prices in March too. Day-ahead gas prices eclipsed the previous record price of 415p/th to sit at 580p/th on 7 March, a likely response to fresh economic and energy related sanctions placed on Russia that morning This fuelled the gas supply shortfall concerns of western economies, as they continue to attempt to reduce reliance on Russian energy imports.

Gas price increases impacted the power market too, with most counterpart contracts mirroring gas price movements.

Elsewhere, day-ahead power prices rose 63% in March, to average just over 313p/th, ~595% higher than the same period of 2021.

Seasonal power contracts from summer 22 to summer 24 rose 21.0% on average in March, a consequence of near-term bullish drivers feeding through to longer dated contracts.

Power contracts for both near-term and longer-term delivery saw strong price rises, primarily driven by the strong upward shift seen in gas counterpart contracts. The day-ahead baseload power contract rose by over 54% in March, to average 262.24p/th, well above 'seasonal norms' and ~337% higher than the same time in 2021.

Some bullish drivers specific to baseload power price rises though, could be seen in the form of a relatively low output month for wind, particularly by comparison to the record outturn levels seen in February.

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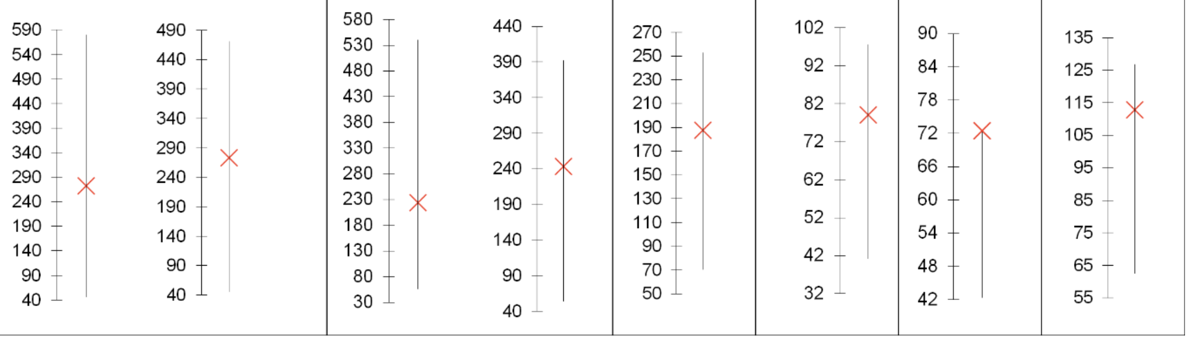
Key market indicators: 29/03/2022

		Gas (p/th)		Electricity (£/MWh)		Coal	EUA Carbon	UKA Carbon	Brent crude
		Day-ahead	Year-ahead	Day-ahead	Year-ahead	($/t)	(€/t)	(£/t)	($/bl)
This month	29 Mar 22	272.00	273.22	224.50	243.50	187.50	79.00	72.50	112.87
Last month	28 Feb 22	260.00	262.63	247.00	240.00	142.00	81.77	79.50	102.89
Last year	30 Mar 21	46.00	44.99	56.00	54.15	72.20	41.16	N/A	64.63
Year-on-year % change		491%	507%	301%	350%	160%	92%	N/A	75%
Year high		580.00	470.47	540.00	392.50	253.00	97.61	87.75	126.84
Year low		46.00	44.99	56.00	54.15	70.65	41.16	42.40	62.44

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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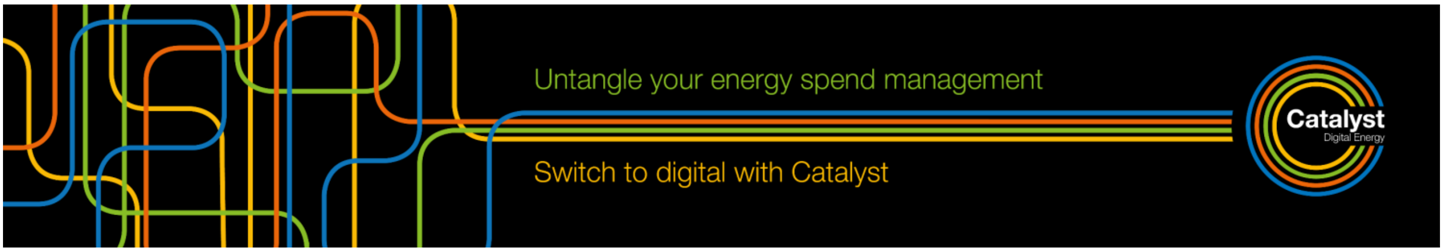


“No clear plan for how net zero transition will be funded”

The Public Accounts Committee published its report Achieving Net zero: follow up on 2 March. The report took evidence from the BEIS, and HM Treasury, on the government’s strategy to achieve net zero by 2050 and how this transition to a green economy will be funded.

Comments from the report stated that there was “no clear plan for how the transition to net zero will be funded” or “how it will replace income from taxes such as fuel duty”, and “no reliable estimate of what the process of implementing the net zero policy is actually likely to cost British consumers, households, businesses or government itself”.

In addition, Dame Meg Hillier MP chair of the Public Accounts Committee, said: “Government is relying heavily on rapidly changing consumer behaviours and technological innovations to drive down the costs of green options, but it is not clear how it will support and encourage consumers to purchase greener products or incentivise businesses and drive change”.

The report outlined a set of recommendations about how things can be improved. These included that the Department and HM Treasury should also set out how it will ensure Parliament can scrutinise the implementation of its net zero policies. This could take the form of annual reports that include the updated costs to 2050 and the amount spent in that year in the public sector to achieve net zero as well as the impact on consumers, households, businesses and local and central government across all sectors and departments and what the expected CO_2 reductions will be. In addition, the department should monitor how quickly technology costs are falling and the levels of private investment it is attracting and set clear triggers for interventions such as new policies and regulations for when things go off course.

Government

Chancellor delivers Spring Statement

On 23 March, the Chancellor Rishi Sunak delivered the Spring Statement 2022 providing an outline of the government’s fiscal plans.

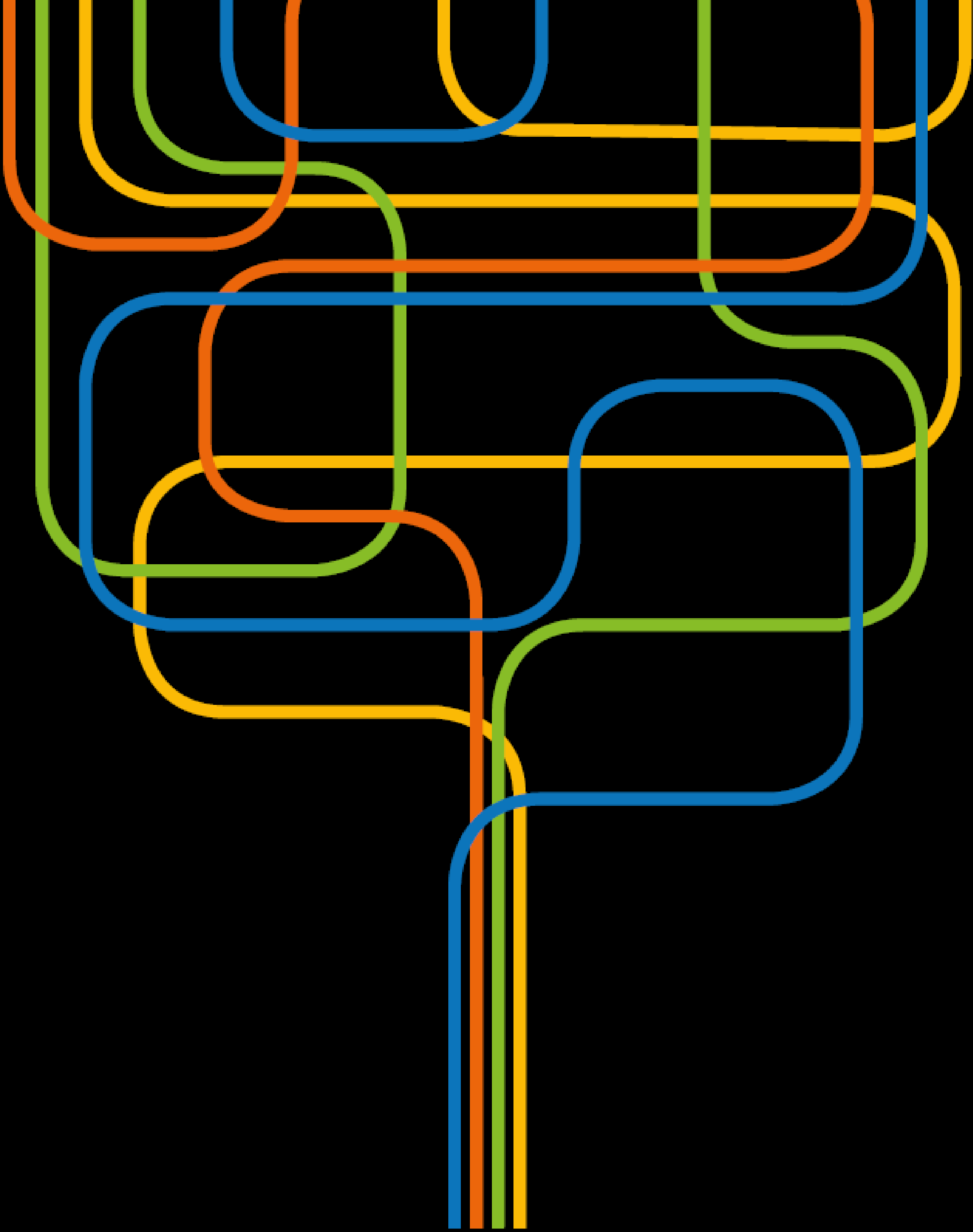
To address the current cost-of-living crisis, the statement highlights the package of support announced prior to the statement in February including the £9.1bn Energy Bills Rebate, designed to provide all domestic electricity customers with an upfront discount on their bills worth £200 – to then be recovered from bills in instalments from 2023.

New commitments included in the statement are plans to remove VAT (previously 5%) on domestic energy saving measures, such as insulation, solar panels, and heat pumps, to help households manage rising energy costs. VAT is also to be removed from wind and water turbines with the technologies to be added to the list of energy saving measures. In both instances, the changes will come into effect from April 2022.

Regarding businesses, the government states it will bring green reliefs for business rates a year forward to April 2022 covering targeted business rate exemptions for eligible plant and machinery used in onsite renewable energy generation and storage, and a 100% relief for eligible low-carbon heat networks with their own rates bill. The statement also includes plans to double the Household Support Fund to £1bn from April and cut the duty on petrol and diesel by 5p per litre for 12 months.

There were concerns that the Spring Statement has not gone far enough to address the ongoing and upcoming impacts of the cost-of-living crisis, with both the Scottish and Welsh Governments reiterating that more vulnerable households will need increased support.

Government



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Brearley calls for reduced exposure to international volatility

On 8 March, Ofgem CEO Jonathan Brearley delivered a speech at the Future of Utilities Smart Energy event, covering the regulator's responses to energy market impacts of the Russian invasion of Ukraine. Brearley said that the invasion underlines the need to move away from fossil fuels, and that it has made GB's existing exposure to extreme volatility and extreme prices even more stark.

It was noted that the situation was unlike anything that had been seen in energy sector in the post-war era and that it represented a second more serious phase of the energy crisis. Ofgem considers that, in the face of increased economic and geopolitical volatility, it is not in the interest of GB consumers to be exposed to international gas markets, and that the energy transition is therefore a transition away from both fossil fuels and volatile prices. Brearley said that although developing gas domestically would support energy security, it would not significantly change prices due to the global nature of markets.

Ofgem

UK to phase out imports of Russian oil due to Ukraine invasion

On 8 March, BEIS announced that the UK will phase out imports of Russian oil in response to the invasion of Ukraine. The phasing out of imports will not be immediate to allow time to adjust supply chains, supporting industry and consumers. The government will work with companies through a new taskforce on oil to support them to make use of this period in finding alternative supplies. The UK is working closely with the US, the EU, and other partners to end the dependence on Russian hydrocarbons. Russian imports account for 8% of total UK oil demand and Russian natural gas, makes up less than 4% of UK gas supply.

Prime Minister Boris Johnson said: "In another economic blow to the Putin regime following their illegal invasion of Ukraine, the UK will move away from dependence on Russian oil throughout this year, building on our severe package of international economic sanctions. Working with industry, we are confident that this can be achieved over the course of the year, providing enough time for companies to adjust and ensuring consumers are protected."

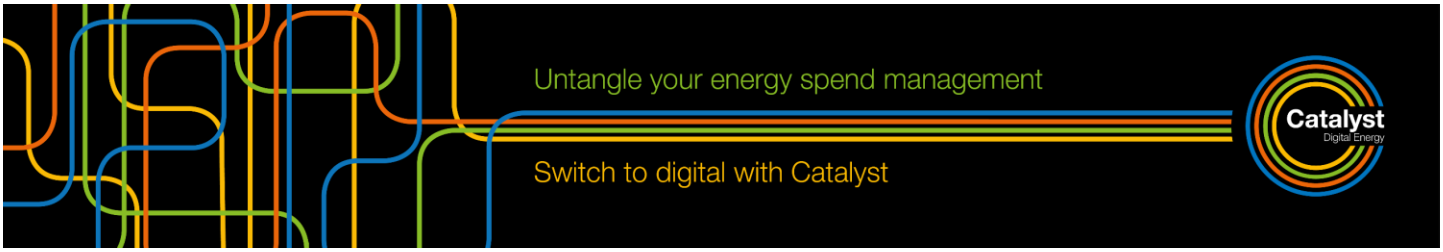
BEIS

Nuclear Finance bill in the House of Lords

On the 24 March members of the Lords began examining the Nuclear Energy (Financing) Bill – which will provide finances for new nuclear power stations by introducing a regulated asset base (RAB). Members put forward amendments to the bill to be discussed, including extending provisions of the bill to nuclear fusion electricity generation, and requiring a geological disposal facility to be operational before a company can be designated as a RAB.

Amendments put forward also include ensuring information is available on the impact the RAB will have on consumer bills, requiring nuclear companies to be either not-for-profit, a cooperative, a Community Interest Company, or wholly owned by UK public authorities to qualify, and establishing a state-owned entity to take over the delivery or operation of a nuclear project if a nuclear company fails and cannot be saved or has its assets transferred.

Government



Plans to extend Winter 22 price cap observation period

On 15 March, Ofgem published guidance on the treatment of wholesale prices observed for price cap period nine (October 2022 - March 2023).

Ofgem's consultation on medium term changes to the Default Tariff Cap closed on 4 March, with the possibility of reducing the implementation period for changes to the cap level from October 2022 among the options considered. While a decision on a new cap mechanism is still pending, Ofgem said that it now has sufficient certainty to delay the price observation window, in line with its policy objectives of shortening the period between price observation and delivery in order to reduce the volume risk faced by suppliers.

It has therefore confirmed that it has decided to proceed with its contingency decision to extend the cap period nine observation window to 31 August, ending one month later than under the existing arrangements. Ofgem stated that it was providing guidance for just the Winter 22 six-month cap period at this point.

The guidance confirmed that as previously committed to, prices observed from 1 February 2022 will be used to calculate the cap level for period nine. Due to the move to a later observation window, with an additional 22 trading days at the end of the period, Ofgem said that it will need to make a "forward-looking change to the price observation profile". It will therefore reduce the weighting of prices while transitioning to the target observation window.

Ofgem

CCC publishes assessment of Heat and Buildings Strategy

On 9 March, the Climate Change Committee (CCC) published an independent assessment of the UK's Heat and Buildings Strategy. It asserts that plans laid out in the strategy are not yet comprehensive or complete, and that significant delivery risks remain. The report from the CCC states that the Heat and Building Strategy sets out the new policy direction, but consultations need to move things forward and then the final design of the policy needs to be completed. This then needs to be followed by effective implementation.

The report highlights five priorities; to fill policy gaps including on home energy efficiency and funding to decarbonise public sector buildings; to build on initial proposals for critical enablers such as skills, information, finance and governance; to strengthen the coordination of the UK strategy with devolved and local plans; to take major strategic decisions, particularly addressing the relative costs of electricity and gas; and to move forward rapidly with the large number of planned consultations and policy papers over the next year, ensuring promising proposals become concrete and timely policy.

The report also highlights several areas which the CCC says should be the mains focus for next steps. This included that around a third of the emissions reductions required in 2035 do not yet have a clear policy plan and/or have significant funding gaps, or it is unclear how the government plans to deliver its targeted ambition.

In addition, funding for public sector buildings decarbonisation up until 2025 currently only covers around a third of what is needed to achieve the government's goal of reducing public sector building emissions by 75% from 2017 to 2037.

The report added that the government has announced consultations which it has yet to initiate, including on owner-occupier energy efficiency, hydrogen-ready boilers and boiler phase-outs for buildings on the gas grid. Plans to rebalance levies between gas and electricity will need to reflect the present circumstances but must make progress to enable the desired shift away from gas in the longer term.

Climate Change Committee

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