



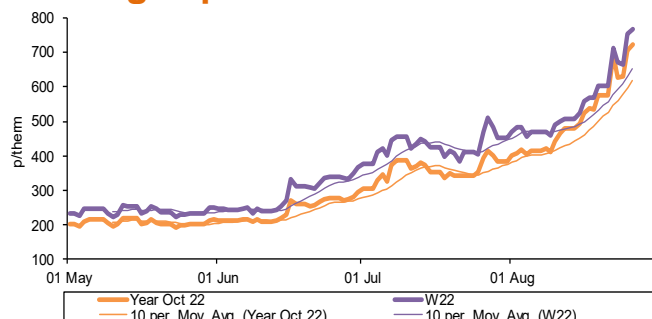
Digital Energy Element

September 2022

Prices hit fresh all-time highs



Annual gas prices



In August, we continued to see strong price rises across all tracked GB wholesale gas contracts in the month. Shorter-term as well as longer dated contracts further out on the forward curve all registered strong bullish price movements from July.

On average, seasonal gas contracts from winter 22 to summer 24 were 58.3% higher in August compared with the previous month. The most significant average price rises concentrated across summer 23 to summer 24 (up 66.9% on average across the three seasons).

The influence of bullish near-term market fundamentals set a strong upward price direction for the forward curve to follow. The sensitive political landscape surrounding westward Nord Stream 1 flows continued to be a dominant market force in August, with flows on the pipeline to Germany meeting just 20% of its total export volume – at a time when European countries continue to refill gas storage facilities in time for the upcoming winter season. August also saw Liquefied Natural Gas (LNG) spot market prices reach all-time highs on our records, with 26 August seeing prices hit 533.22p/th – a factor influencing both European and GB wholesale gas prices, with LNG acting as a marginal price setter.

As a result of the aforementioned bullish drivers for gas prices, we saw day-ahead gas climb strongly, up 56.2% on average from July to sit at 374.48p/th. Front-seasonal contracts also shared collective average price growth, with September 22 up 24.8% to 435.62p/th and October 22 rising 29.3% to average 490.46p/th.

We also observed record highs on the front-seasonal gas contract (winter 22), which hit 766.55p/th on 26 August, dwarfing the previous record set in July 2022 (469.90p/th).

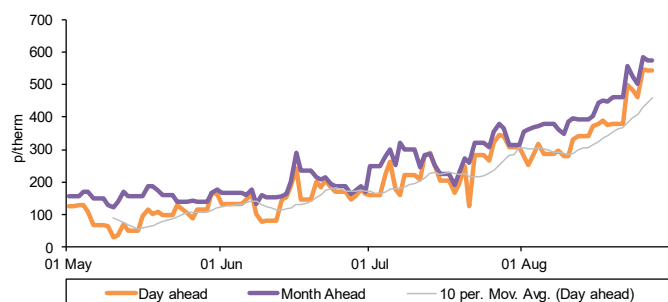
August saw day-ahead power prices follow their gas counterpart upwards – 44.1% higher on average to sit at £382.43/MWh. This represents a 252.0% rise compared to prices from the same period in 2021.

The strong upward momentum on near-term domestic gas prices set a bullish direction for power prices to follow. The continuation of higher levels of exports via our interconnectors to Europe remained prevalent in August, as interconnected markets such as France continues to observe higher power prices compared with GB on average.

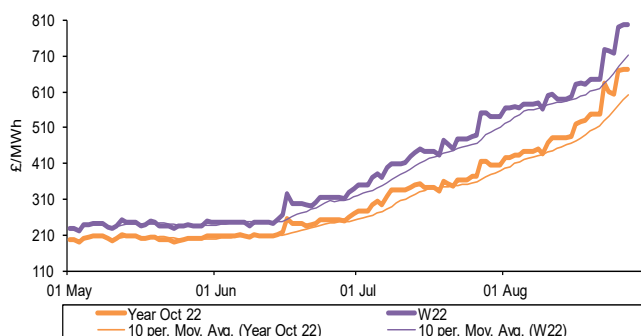
Front-month power contracts (September and October 22) shared the price direction of their gas counterparts and day-ahead power prices, subsequently rising 27.0% on average to sit at £408.09/MWh and £477.00/MWh, respectively.

Commodity markets primarily saw the continuation of elevated price points, continuing to be unsettled by developments from the Russia-Ukraine war and winter supply fears. Both the UK and EU ETS carbon markets rose in August – up 8.5% to £88.20/t and 5.0% to €86.00/t respectively. Higher cooling demand during the prolonged heatwave period in the UK and Europe helped prices climb on average in the month. Elsewhere, Brent crude prices slipped 7.1% to \$97.52/bl.

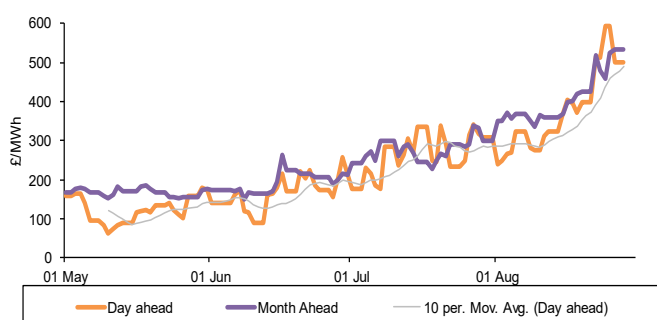
Spot gas prices



Annual power prices



Spot power prices





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Key market indicators: 31/08/2022

| | | Gas (p/th) | | Electricity (£/MWh) | | Coal (\$/t) | EUA Carbon (€/t) | UKA Carbon (£/t) | Brent crude (\$/bl) |
|-----------------------|-----------|------------|------------|---------------------|------------|-------------|------------------|------------------|---------------------|
| | | Day-ahead | Year-ahead | Day-ahead | Year-ahead | | | | |
| This month | 31 Aug 22 | 405.00 | 0.00 | 465.00 | 0.00 | 302.00 | 80.53 | 92.65 | 96.02 |
| Last month | 3 Aug 22 | 285.00 | 0.00 | 266.00 | 0.00 | 285.00 | 78.35 | 81.00 | 99.27 |
| Last year | 1 Sep 21 | 133.00 | 76.91 | 147.00 | 104.44 | 118.50 | 61.40 | 52.50 | 71.75 |
| Year-on-year % change | | 205% | (100%) | 216% | (100%) | 155% | 31% | 76% | 34% |
| Year high | | 580.00 | 470.47 | 595.00 | 189.00 | 333.00 | 97.61 | 97.00 | 126.84 |
| Year low | | 28.00 | 76.05 | 63.00 | 103.00 | 97.60 | 55.85 | 51.75 | 70.50 |

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.

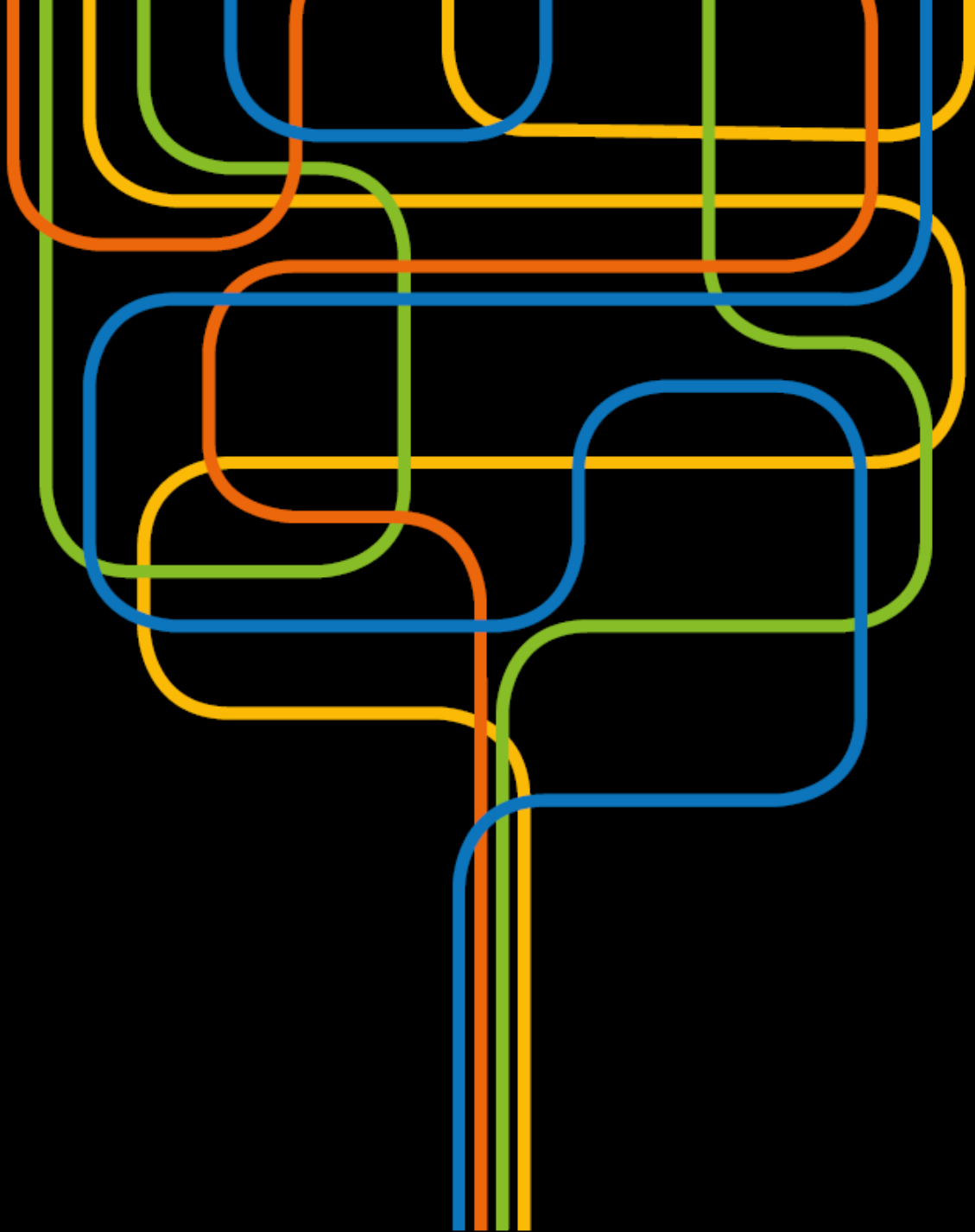
Margin: The indicated UK imbalance of a given settlement period. It is the difference between the sum of the indicated generation available, and the national demand forecast made by National Grid.

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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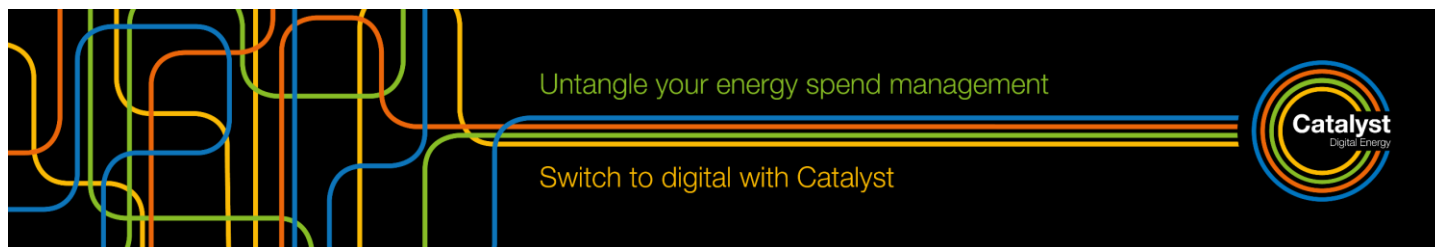


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Changes to Default Tariff Cap methodology published

On 4 August, Ofgem published several decisions on changes to the Default Tariff Cap methodology ahead of winter 2022-23. This includes its decision on changes to the cap wholesale methodology, including moving from six-monthly cap updates to quarterly cap updates and a reduced notice period of 30 working days. This decision also introduced a mechanism for recovery of backwardation costs over six-months into the methodology. To accompany this the regulator published updated guidance on the treatment of price indexation in future cap periods.

In addition to this update, Ofgem published its decision to update the smart metering allowances for credit and prepayment (PPM) meters in the cap for cap period nine and has set the allowance for credit Smart Metering Net Cost Change (SMNCC) at £9.37 and the PPM SMNCC at -£28.69 per typical dual fuel customer. It has also decided to apply an adjustment to the cap for non-prepayment meter (non-PPM) customers to account for unexpected standard variable tariff (SVT) demand costs incurred by suppliers over cap period eight, but decided not to adjust for cap period nine or for shaping and imbalance costs across either period.

These changes will take effect at the beginning of the next cap period on 1 October 2022. Furthermore, the regulator gave notice of a delay to its decision on the COVID-19 true-up process and debt-related costs.

Ofgem

BEIS consults on proposed increase to EII subsidy relief

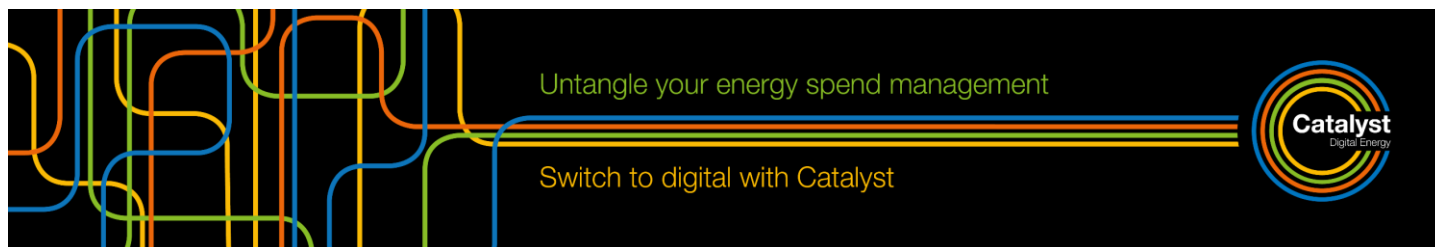
On 12 August, BEIS released a consultation seeking to review the energy intensive industries (EII) exemption scheme to consider whether there is a rationale for increased measures to mitigate the costs from renewable electricity policies for high electricity using businesses.

Under the current EII exemption scheme, high electricity using businesses, such as steel and paper mills, see a proportion of their costs relating to the Contracts for Difference (CfD), Renewables Obligation (RO), and Feed-in Tariff (FiT) made exempt. The EII scheme is designed to keep these industries internationally competitive by preventing electricity policy costs significantly adding to energy bills compared with those in other international jurisdictions. It also aims to limit the risk of carbon leakage where additional costs could discourage electrification of manufacturing processes and slow progress towards the UK's net zero target.

The costs of funding the CfD, RO, and FiT schemes are recovered through obligations and levies placed on electricity suppliers, which are ultimately passed on to consumers through electricity bills. The EII exemption scheme currently provides a discount of up to 85% of the indirect costs of these support schemes, with the exempted costs then distributed among the remaining eligible consumers. However, following a commitment in its recent Energy Security Strategy, the government is proposing to increase the level of exemption from 85% of environmental and policy costs up to 100%, which would see prices for EII eligible companies potentially fall more into line with the EU-14 average. In its current form, the scheme reduces net electricity prices for EIIs by between £19/MWh and £37/MWh on average. A 95% subsidy intensity would see a reduction in average electricity costs of between £23/MWh-£37/MWh for eligible EII firms, while a 100% reduction would see a reduction of between £34/MWh-£38/MWh. However, it is noted that a subsidy intensity of 100% may lessen the incentive for businesses to invest in energy efficiency, which would support businesses to reduce their energy bills and emissions in the longer term.

Responses are requested by 16 September 2022.

BEIS



NGESO publishes early view of winter 2022-23

On 28 July, National Grid ESO (NGESO) published its early view of winter 2022-23 in an aim to provide the electricity industry adequate time to prepare for the coming winter.

NGESO notes that a detailed analysis will be presented in the winter outlook report which will be published in the autumn. It states that it is operating under the assumption that the peak demand on an average cold spell will be 59.5GW on the transmission and distribution networks, including a 1.2GW reserve. The base case assumes normal market conditions and that there may be some tight periods, but it is expected they are able to be managed using standard operational tools.

It also adds that it is taking actions to build resilience to potential risks and uncertainties due to a possible shortage of gas supply in Europe. These include delaying the closure of two coal power stations, with a combined five units, which together can deliver 2GW de-rated capacity. Currently, four of the five units have confirmed their availability. NGESO has not included these units in the base case margin assumptions as they will not be available in the market, instead they are additional. NGESO is also considering options to increase the incentives for electricity customers to participate in the demand side response.

NGESO

Ofgem confirms price cap increase for winter at £3,549

On 26 August, Ofgem published its decision confirming an 80% increase to the Default Tariff Cap, since the last update, to £3,549 for the upcoming cap period (9a), covering 1 October 2022 – 31 December 2022. This figure applies to a typical direct debit dual fuel customer.

For other payment types, the standard credit cap has increased to £3,764, and the prepayment meter (PPM) cap level has increased to £3,608. The regulator provides a breakdown on what has caused the increase in the cap, including the increase in wholesale costs primarily due to the Russian invasion of Ukraine, more volatility, and backwardation costs.

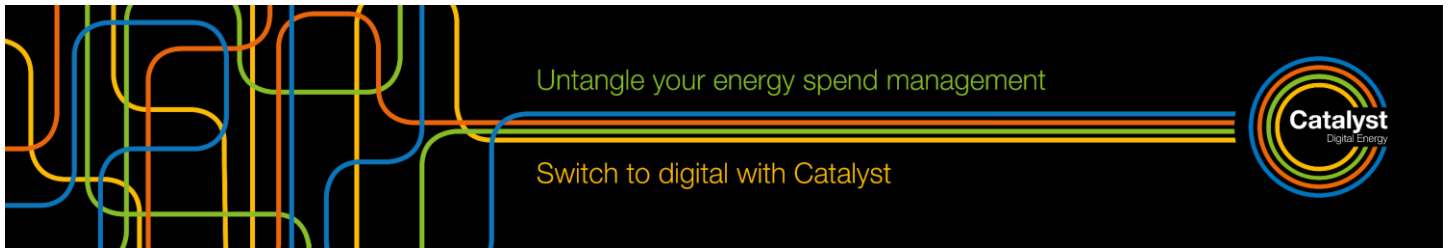
Ofgem

Views sought on power CCUS future policy framework

On 25 July, the government published its Future policy framework for power with carbon capture, usage and storage (CCUS): call for evidence, seeking views and evidence on how it can best support the continued deployment of dispatchable gas-fired power generation with CCUS projects into the 2030s beyond Track-1 of the Cluster Sequencing process. This includes how the CCUS business model should be evolved over time, how competitive allocation can be introduced in the 2020s, the removal of barriers to deployment, how economic benefits can be maximised through future policies, how the power CCUS sector is expected to develop, and how power CCUS could work with wider electricity markets, taking account of the recent Review of the Electricity Market Arrangements (REMA) consultation.

Responses are requested by 17 October and will help inform the policy framework for power CCUS as well as feed into other policy initiatives, such as REMA.

BEIS



Phase 3 of ESOS to increase energy and carbon savings

On 28 July, BEIS published the outcome of its consultation Strengthening the Energy Savings Opportunity Scheme (ESOS), which is a mandatory energy assessment scheme for organisations in the UK that meet the qualification criteria. It stated that there was widespread support for the proposals to increase energy and carbon savings for those that participate in ESOS.

Proposals to be adopted for Phase 3 include:

- A standardised template for including compliance information in the ESOS report.
- The reduction of the 10% de minimis exemption to up to 5%.
- The addition of an energy intensity metric in ESOS reports.
- Requirement to share ESOS reports with subsidiaries.
- Requirement for ESOS reports to provide more information on next steps for implementing recommendations.
- Requirement for participants to set a target or action plan following the Phase 3 compliance deadline, on which they will be required to report against for Phase 4.
- Collection of additional data for compliance monitoring and enforcement.

The document also sets out a summary of feedback received on two further options, which will inform developments in future phases. This includes extending the scope of the scheme to include medium-sized businesses, not already part of a corporate group containing a large business, and mandating action on audit recommendations.

BEIS

Long range electricity storage policy to be developed

On 3 August, the government published the outcome of its July 2021 call for evidence on Facilitating the deployment of large-scale and long-duration electricity storage (LLES).

Having reviewed the responses, and externally commissioned analysis, it set out several conclusions that have been reached in relation to LLES. This includes that it has an important role to play in achieving net zero, as it will help to integrate renewables, maximising their use and contribution to security of supply. It will also help to manage constraints in certain areas. The consultation outcome adds that it also provides low carbon flexibility, replacing some unabated gas generation. In addition, it will diversify the technology mix and support meeting the 2035 decarbonation power sector targets. It also highlighted barriers to deployment citing the current market framework due to their high upfront costs and a lack of forecastable revenue streams.

As such, the government confirmed that it will ensure the deployment of sufficient LLES to balance the overall system by developing appropriate policy to enable investment by 2024. While most respondents identified a cap and floor type mechanism as the most suitable to enable investment in LLES, the government said that detailed design work is needed to assess the benefits and interactions of such a scheme with the energy system.

It added that it will carry out further analysis on the costs and benefits of intervention in the market for LLES, including its contribution to energy security and possible market distortions. It will also consider options including a cap and floor, and an optimised Capacity Market in addition to wider flexibility operational signal sharpening being considered under the Review of Electricity Market Arrangements (REMA). In addition, it will work with Ofgem to develop an appropriate policy to enable investment in LLES.

BEIS



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