Energy security: a picture of uncertainty

By Grace Segran

Uncertainty surrounds the security and sustainability of energy supplies in the UK from 2015 onwards, with energy prices rising – in some cases – to uncomfortably high levels. “Gas would be a very important bridge to take us to the Elysian fields of a much cleaner energy scene of onshore and offshore wind, renewables, and an expectation of a very large chunk of nuclear,” says Alistair Buchanan, Chief Executive of Ofgem (the Office of the Gas and Electricity Markets), speaking at The Economist’s recent UK Energy Summit.

These were the conclusions of Project Discovery, Ofgem’s year-long investigation into whether secure electricity and gas supplies can be delivered by existing market arrangements. Its medium-term review into electricity and gas supplies in the UK over the next 10 to 15 years was driven by what Buchanan calls the ‘unholy trinity’ of credit and carbon crises, and Britain’s position in the global gas market, with its associated macro-political implications.

Delays and strategies

Today we see substantial delays in developing gasfields. The giant Shtokman field in Russia's Barents Sea and the Nabucco pipeline are not coming online as originally envisaged. LNG (liquefied natural gas) facilities within Europe are also facing delays, with Croatia and France announcing delays in the last couple of months. “We expect Euro shale to be the answer until we get comfortably into the 2020s and possibly a bit further out from that,” says Buchanan.

In addition, Buchanan says that it’s worth looking at the key gas companies within Europe’s strategy this year, in particular Gazprom, as they have locked in major long-term contracts with Poland, Ukraine, Slovakia, Austria, Germany and the Netherlands.

With regards to the pricing strategy of the major players, the chief executive of Gazprom and the Energy minister of Qatar have both confirmed recently that they are not keen to see a delinking of gas and oil prices.

Project Discovery assumes a full move to US shale and if indeed that is the case, then there is a need to look very carefully at the US in detail to see whether there is any kind of coal-gas switch, and what the implications are both in terms of the environment and the scenario following the BP oil spill in the Gulf of Mexico.

“The picture I am trying to paint is that we could go from a feast to a famine within a decade based on a number of certain scenarios – or we might not,” says Buchanan. “But it is into this picture of uncertainty that the government, led by Chris Huhne (Secretary of State) in the Department of Energy and Climate Change, have decided to pursue rapidly in the agenda on energy markets reform, focused on the electricity side and a gas security supply answer. And we’ve got to watch very carefully the next year and welcome the government’s policy deliberations in these critical areas.”

With the oil spill in the Gulf of Mexico, along with the financial crisis and the slow progress in talks on climate change and millennium development goals, there is likely to be more, rather than less, pressure towards frameworks, government intervention and regulation, **Christoph Frei**, Secretary General of the World Energy Council (WEC) told INSEAD Knowledge on the sidelines of the summit. “In that context, it is even more important to review policies

and separate the wheat from the chaff."
According to Frei, a number of unsuccessful policies have been implemented in the past and the WEC has reviewed more than 230 individual policies over the past 12 months and is now preparing its conclusions. One of these is that renewable energy policy frameworks need to be reviewed regularly to ensure investment momentum is maintained, implementation fully achieved and programmes are responsive to changing market conditions. Caps should be raised on renewables take-up to encourage continued investment, while economic limits should be set on installed capacity and tariffs should be reduced from time to time to avoid windfall profits and additional costs to consumers.

In terms of security and risk profile, International Power, an independent power generation company, is focused on the regulatory risks across its markets. **Philip Cox**, its Chief Executive, compares the process to finding equilibrium between the security and affordability of energy supplies, and carbon reduction.

"The bigger risk factor that we see is how the regulatory requirement in different markets is trying to piece together those three, sometimes very competing drivers. So clarity, consistency, fair-mindedness, long-term vision, evolutionary not revolutionary – all these guiding principles from a regulatory point of view are very important to us."

What International Power would like to see is a level playing field for all technologies. Cox says there's room for coal, gas, nuclear and renewables, but would like to see a more balanced approach, rather than incentive packages targeted at specific fuels or technologies.

"We'd rather be in the field of lower incentives. We are in favour of incentives that are already in, on which investment decisions have been made, and need to be kept. We are in a long-term, high capital-intensive industry where decisions need 20, 30, 40 years to get the payback. So changing those retrospectively is not something we are in favour of at all, but we are wary of introducing a new level of complexity in terms of incentives which incentivise one technology at the expense of another," he argues.

For example, if a company is thinking of building a gas-fired plant in the UK to come online in 2015, at just about the time when the potential squeeze on reserve margins in the UK are getting intense, it would be ‘very worried’ about making that decision if it felt there may be an incentivised nuclear plan down the track in, say, 2020, Cox says. “The overarching point is that, as a generator that lives in both regulated and liberalised markets, we are a big proponent of free, open, accessible, competitive markets which is broadly what we’ve got in the UK and that’s what we’d like to see going forward,” Cox says.

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