

CRIPPS SEARS & PARTNERS

40 | CELEBRATING FORTY
YEARS OF SUCCESS

Energy Executive Network Lunch

06.10.16

Brexit

Since the last Energy Executive Networking Forum six months ago, the Brexit referendum has been held and members were keen to share views. It was suggested that many Europeans, though initially disappointed by the result, don't much care now and would leave matters to politicians. Frankfurt was looking forward to an upsurge in business: some industrialists were less enthusiastic. There was likely to be a hiatus on investments; and some sectors have come to depend on European labour. What would be the new 'business model' for UK plc?

It seemed likely that part of the answer would be: *trade off the cheap pound, and borrow*. The decline in Sterling may offset new tariffs on British exports: but inflation may also result. The transition would take ten years.

Chancellor Merkel was unlikely to be able to steer the Brexit negotiations: there are elections coming, and Germany doesn't wish to be seen driving such issues. On the European side, the clear goal would be to ensure the UK is worse off than if it had remained – otherwise there would be disintegration in the EU. (Already, 'populist' policies were being seen across Europe; border restrictions, etc.) This being the case, the UK side would quickly need to factor in a hard landing in any circumstances, and 'do whatever it takes' – becoming a Hong Kong of Europe, for example.

Hinkley and New Nuclear ...

... another topic with a Brexit angle. Hinkley had been given the go-ahead drive by the UK's need to be seen as open for business. The project was based on politics, not economics – as with other European energy initiatives, e.g. the *Energiewende*. Hence, Centrica had pulled out some while ago, writing off substantial expenditure. The investment approach was the 'PFI hospital' model, based on arbitrary separation of capital and revenue accounts.

Building a 'first-and-last-of-a-kind' EPR was inevitably risky and costly. The UK and France actually had plenty of time to wait and see what new and better alternative nuclear designs became available: power prices of £65-70 should be possible. The EPR is akin to Concorde, when what is needed is an Airbus.

Was EDF lucky to get UK approval? One view was that in fact it represents a free option for the UK (the opposite of how some UK observers see it!) because a 35-year contract starting perhaps 10 or more years in the future would never stick; and the 2025 start-up 'target date' was unachievable. Thus, inevitably the deal will be renegotiated. It was asked whether Chinese involvement had de-risked the project for EDF: but it was suggested that China's exposure is bounded, and so the substantial construction risk lies essentially with EDF.

CRIPPS SEARS & PARTNERS

40 | CELEBRATING FORTY YEARS OF SUCCESS

Members with interests in the South West of England noted that for hoteliers and property-owners the 10-year Hinkley construction project will bring a local boom!

The question was then raised: what will fill the gap between today's rapidly closing UK coal capacity, and a future period when viable new nuclear could come onstream? Gas was the obvious candidate (the 2 GW of open-cycle diesel capacity was caustically also mentioned), but how could it be financed? It was suggested that the already-existing Capacity Mechanism will be manipulated to make available a bankable revenue stream sufficiently large as to make new CCGT projects viable. It was also noted that gas prices were currently low (the result of a surplus of LNG) and that spark spreads were rapidly recovering.

It was suggested that the economics of new coal plant could also be viable – if built over the pit, in Germany – but that this was becoming politically unacceptable, notwithstanding the favourable light in which coal has been seen in Germany for its rôle in post-war economic development. The cost of long-distance coal imports was too high to be an alternative.

Was social pressure for a CO₂-free economy 'real'? It was suggested that this only existed while the lights stayed on, but that security of supply would always ultimately prevail as a political imperative. Geo-engineering was mentioned as an alternative to constantly focusing on decarbonizing the power sector as the 'solution' to global warming. The role of increases in population was also mentioned. Where would strategic decision-making come from? The decision timeframe for politicians was 4-5 years at most; and it was not much longer for corporate management, the average CEO being in office only 5-6 years.

It was suggested that in Europe, the main strategic solution would be further large-scale reductions in demand. However, the lack of political will to enforce existing regulations (for example, the very demanding building insulation rules in Hamburg) was noted. Some also observed that in reality the actions of Europe were substantially less relevant than those of China, India and the USA.

Oil Price

Given market movements since the start of the year, is the oil price now set to rise? It was noted that in many countries the consumer is shielded from the market price of oil by immense subsidies, suggesting that there is scope for significant efficiencies and demand reduction yet to be made. Also, technology was still capable of delivering further step-changes in efficiency, both in production and at the point of use. All of this would speak to downward pressure on the oil price.

The potential of shale resources was mentioned as another factor bearing down on oil (and gas) prices: it was implausible that the USA was the only region with shale oil. How this would be affected by water-related issues? It was stated that any region where sea-water was accessible (e.g. the UK, Algeria) would have no problems on the fracking aspect. As regards polluting the water-table, provided the well casings were completed to a high standard this too was not a technical problem – albeit that in some States of the USA, environmental standards were very lax on such matters. If shale resources were present in the quantities some claim, there could be no objection to tight regulations.

CRIPPS SEARS & PARTNERS

40 | CELEBRATING FORTY YEARS OF SUCCESS

On the other side of the technology argument, some felt that advances also increased prosperity in countries such as China and India, which would create many more people wanting to become owners and drivers of cars. Discussion of motoring passed to the relative merits of the current generation of electric cars – often not very energy-efficient, even if highly tax-efficient!

The next Energy Executive Forum will be

NP October 2016