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European Energy Infrastructure Networking Forum 23 February 2017

Subsidy regime and finance in UK

Discussion started with the question of how investable the UK would be as various subsidy regimes were coming to an end. The UK had been favourably viewed in the past. From the government's point of view, the cost of renewables was falling to the point where subsidy was no longer 'required'; but merchant assets did not have the same risk profile as 'infrastructure' and for some classes of investors this would be critical.

This said, it was pointed out that there was a large pool of liquidity seeking yield: a recent acquisition of UK solar assets by EFG Hermes and TNB (Malaysia) at a significant premium was cited. Scarcity value attached to remaining ROC-based assets. Also, if one looked (e.g.) to the USA where utility rates strongly followed long bonds – what was the alternative investment?

The view was expressed that there was no longer a proper UK energy policy, and that events were being driven by private interests doing their thing. Was a stream of capacity payments investable? Yes – but as a proportion of the total capital requirement it was relatively small, at the clearing prices seen thus far in the UK Capacity Mechanism.

A shift away from large centralised powergen projects towards decentralised / distributed generation. This new class of assets attracted a different class of investor. Also, initially, there were likely to be specialised early investor / aggregators who would package assets for more traditional investors to come in further down the road.

Rooftop solar made a lot of sense in, e.g. India – but other issues would arise there for investors. "What is needed is a power price spike in the UK" !

A future role for CCGTs?

Could a role be defined for CCGTs in the future UK energy mix? Yes – but not at the capacity prices currently prevailing. It was noted that Macquarie, and before them Centrica, had both taken speculative long positions in CCGT capacity, but that in recent times that bet was not paying off. However, OCGTs (new-build, of fairly large size) had been successful in the capacity auctions.

There was an element of 'fashion' as to whether merchant CCGTs could be financed. In the early 1990's, only a full hedged 15-year gas-power position was good enough to get an IPP away. However, as the '90's progressed an ever greater proportion of merchant capacity became acceptable.

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Might interconnectors be a substitute for new-build capacity? It was noted that many countries around Europe were increasingly relying on interconnectors, but that when the going gets difficult there could simply be not enough physical energy available. In this connection there was discussion of whether Brexit would result in new problems for cross-border energy movements.

Nuclear power, tidal power ...

The potential contributions of nuclear and tidal to the UK energy mix were discussed. It was suggested that at least nuclear power was already permitted and, to a large extent, publicly accepted. It was also offering baseload electricity. Tidal generation, although predictable, could not in practice deliver baseload. Additionally, the permitting issues were large and unresolved, with potentially significant environmental aspects and corresponding challenges for achieving public acceptance.

If traditional large-scale nuclear power was running into difficulties, perhaps small modular reactors (SMRs) might prove more attractive? Moltex, a firm seeking to develop 'molten salt' technology was mentioned. This technology could come in at less than the cost of new coal-fired power; and the UK government was running a competition for SMR proposals. However, it was reported that the ONR was inundated with work relating to Hinkley, Moorside and Wylfa, and had insufficient time to consider SMR issues in detail. Moltex was considering switching its attentions to Canada, where regulators had more bandwidth. Rolls Royce was also cited as a company with interests in SMR – but they were hindered by their inability for legal / security reasons to utilize directly their experience with small nuclear reactors in Royal Navy submarines.

It was suggested that the big problem for SMRs would be NIMBYism. The business case for SMR was that district heating would be involved, and the reactors would therefore be sited near centres of population – and who wanted one in their town?

The Big 6 and other energy suppliers

The reputed shortcomings of the Big 6 were rehearsed: not at all agile; struggling with the basics; very bad at billing, and at systems and customer relations generally. With that backdrop, wasn't there great scope for smaller, more customer-focused suppliers to thrive? They could have clear advantages in chosen specialist areas such as trading, CRM, forecasting etc.

It was generally agreed, however, that there were several reasons why this might not work out in the long run, either in the UK, or the USA where some participants had experience. Customer switching in practice was very low (as evidenced by a straw poll around the table). Until smart metering became ubiquitous, all companies would have difficulties in billing effectively. The Big 6 could cross-subsidise selected customers from their large standard variable tariff (SVT) base, in a way new entrants could not match.

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It was always possible for new players to price their way to the top of the comparison-site rankings, and to win market share in times of falling wholesale prices. However, as soon as prices ticked up, they would founder: the barrier to entry (cost of a licence) was very low and many were under-capitalised, with inadequate working capital and no ability to hedge. The recent case of GB Energy was cited, along with other small suppliers whose growth had levelled off. It was also noted that the government leans heavily on the Big 6 for implementation of many aspects of policy. There may be room for 2 or 3 'independent suppliers' long-term, but most of the Big 6 would probably survive.

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23 Feb 17