

The Fourth Annual Fuellers' Energy Lecture

European Energy Policy



Presented at the offices of S J Berwin LLP
on the evening of
Wednesday 7th May 2008

by

Lord Browne of Madingley

Master, Wardens, Masters of Livery Companies, My Lords, Ladies and Gentlemen.

It's a tremendous honour to be here to deliver the fourth annual Fuellers Lecture, following in the distinguished footsteps of Lord Ezra, John Harris and Sir Bernhard Ingham.

I've been asked to speak today about European energy policy.

Five years ago, this would have been seen as a rather esoteric subject.

Today, it could not be more relevant. The nexus between energy, the environment – and now food – has become one of the most talked about issues of our day.

I'd like to begin my remarks this evening by laying out the broad drivers that I see underpinning energy in Europe today.

And I think a good place to start is the Reform Treaty which was signed by European heads of state in Lisbon last December.

That document enshrines three goals at the heart of EU energy policy:

- Economic competitiveness and growth;
- Energy security;
- And – for the first time in a cornerstone European text – combating climate change

Promoting competitiveness and growth has, of course, been a constant in European energy policy – as it is for all governments.

Energy security and climate change, on the other hand, have arrived on the political agenda rather more recently.

It sometimes takes a sudden, dramatic moment to reveal fundamental change. And such a moment occurred in the first few days of 2006, when Russia decided to cut off its gas supplies to the Ukraine.

That event highlighted Europe's dependence on increasingly concentrated hydrocarbon supplies from outside its borders – a dependence that's expected to increase rather than diminish over time. The Commission estimates that the EU could import more than 80% of its gas and more than 90% of its oil by 2030.

Whereas energy security arrived on the political agenda in a clap of thunder two years ago, climate change has emerged through a steady crescendo over the past decade or so.

The scientific evidence that manmade climate change is occurring and could have dramatic impacts on human activity has grown increasingly compelling. Public concern is mounting.

And in response, Europe has established itself as a global leader in climate change efforts:

- The EU possesses the world's first and largest carbon cap and trade scheme, which – under proposals announced in January – will be strengthened considerably in the years ahead
- It has adopted the most ambitious greenhouse gas reduction targets – 20% by 2020, rising to 30% if there is an international agreement
- And the EU has become a leading advocate for an international climate change framework to replace the Kyoto Protocol – a position cemented during last December's Bali negotiations.

It seems to me that growth and competitiveness; energy security; and tackling climate change are the *right* three goals for European energy policy in the post-Lisbon world.

However, the picture is complicated – because these three goals are not always congruous with another. There are tradeoffs between them.

A good example is the choice about whether to build more gas- or more coal-fired generation, in response to rising electricity demand or to replace retiring plants.

Gas emits half the CO₂ per unit of power generated compared with coal, so replacing coal plants with gas-fired alternatives is an important route to lowering emissions. The so-called 'dash for gas' in the late 1990s is the main reason why Britain is on track to meet its emissions reduction targets under the Kyoto Protocol.

Yet there is a tradeoff with energy security.

In the UK, the increasing importance of gas in our energy mix has also increased our reliance on foreign energy imports, because of the decline in North Sea gas reserves.

Another example of a tradeoff between the three overarching energy goals is the introduction of carbon pricing.

As Lord Stern and many others have argued, the introduction of a robust, long-term carbon pricing signal is by far the most important policy instrument available to combat rising emissions.

Yet pricing carbon will also, inevitably, impose a cost on energy-intensive sectors.

This is leading to growing fears that European industry will lose its competitive position – particularly in those sectors that, under new rules, will have to buy their carbon permits rather than being awarded them for free.

Looking at these and the many other energy tradeoffs, I am struck by the uncertainty and complexity of the current situation.

To use a nautical metaphor, we seem to be in the midst of swirling currents. And in such a world, I believe European policymakers need beacons, fixed principles to help them navigate.

I'd like to propose four such principles this evening.

The first is that European energy policy should be conducted on a cross-border basis.

Put simply, I believe Europe's most pressing energy challenges are best addressed by Member States working together rather than separately.

This is the concept of 'solidarity' – a word that features prominently in the energy passage of the Lisbon text.

A good example of where a collective approach is called for is in energy infrastructure.

A more flexible, cross-border electricity grid would make the delivery of power far more efficient, reducing overall consumption and lowering costs.

It would also allow greater penetration of intermittent renewable energy sources such as wind and solar.

Another example of where a cross-border approach would pay dividends is in strengthening and extending pan-European trading schemes.

Market mechanisms are unparalleled in their ability to allocate public goods efficiently. A strengthened EU ETS – in conjunction with a new renewable electricity trading scheme – would allow the EU to reduce emissions and diversify energy supplies at lowest cost.

That means including *all* sources of CO₂ reduction – notably credits from forestry, which are currently banned.

And it means improving the way the EU ETS is governed, in order to reduce short-term uncertainty and avoid moving the market by press release.

The second principle is the need for better data.

It is deeply concerning that many discussions about energy, and renewable energy in particular, seem to be taking place in a fact-free zone.

Biofuels is a good example.

To say recent media coverage has been alarmist is an understatement. Biofuels are being blamed for rocketing food prices, rampant deforestation and for being at best carbon neutral.

These claims do not help. The situation requires more detailed analysis.

There *are* bad biofuels. But there are also many *good* biofuels. And the facts show that the best ones, like ethanol from Brazilian sugarcane, have no impact on food, aren't responsible for deforestation and can result in significant carbon savings.

The recent surge in the cost of rice – a staple for developing countries in east and southeast Asia – should be of particular concern. But that has nothing whatsoever to do with biofuels.

The European Commission is making important strides in defining practical biofuels standards. And I remain hopeful that this sensible, fact-based approach will prevail over political posturing.

Another example of an unsupported claim is the argument that consumers will be crippled by the introduction of carbon pricing.

A simple calculation shows that even a hundred dollar CO₂ price would cause petrol prices to rise by just 13 pence per litre here in Britain. To put things in perspective, that's 4p less than the 17p increase that's occurred in the last 12 months.

The third principle to guide European energy policy is promoting new technologies.

Diversifying energy supplies and reducing emissions will be impossible unless Europe promotes the rapid development of new energy technologies.

Doing this will first require removing barriers, such as eliminating subsidies for conventional energy sources and improving grid access for low-carbon electricity plants.

It will also require streamlining Europe's cumbersome planning laws. Currently, renewable power plants have to gain approval from an average of 9.5 authorities before they can be built.

Another barrier, especially for new technologies such as carbon capture and storage, is public education.

As well as removing barriers, deploying low-carbon technologies at scale will require stable fiscal and regulatory incentives.

In the long term, a carbon price will be sufficient. In the short- to medium-term, low-carbon technologies will need transitional support – in the form of feed-in-tariffs, quotas, tax breaks and other tailored incentives.

Such incentives should be designed to accelerate low-carbon technology cost reductions, bringing forward the point such technologies can compete with just a carbon price.

The application of new technology, such as modified vehicle engine systems, will be particularly important in harvesting energy efficiency savings. These are estimated to be worth at least 60 billion euros per year across the EU – equivalent to 20% of EU energy consumption and translating to hundreds of millions of tonnes of carbon emissions

Of course, driving energy efficiency will also require changing consumer behaviour – and I believe European governments need to do much more in this regard.

The fourth and final principle I'd like to talk about this evening is the importance of global leadership.

My remarks so far have focused on actions within European borders.

But I believe that Europe does outside its borders – on the global stage – will be just as important. That's particularly true for today's most pressing energy challenge: combating climate change.

We face a stark fact: cutting emissions by the necessary amount will be impossible without coordinated, global action that encompasses developing nations.

The core elements of such an agreement must include:

- First, a long-term, binding emissions cap and a trajectory for achieving it;
- Second, a burden sharing agreement that defines regional and national responsibilities;
- Third, a global carbon pricing mechanism;
- Fourth, a policy framework to encourage technology transfer;
- And fifth, incentives to tackle the critical issues of deforestation and land use change, which are responsible for around 20% of global emissions today

Establishing each of these components will entail difficult political negotiations.

There are highly emotive equity issues at stake – particularly the question of how much responsibility developing countries should bear.

Yet I believe Europe could make a tremendous difference here.

As a global first mover on climate change targets, the EU has the credibility to be a leader in international negotiations.

And as the first region to have adopted an international carbon trading system, it has the practical experience.

Europe also has important *political* experience. It is used to operating in a world of overlapping sovereignty, to striking a balance between supranational institutions and Member State governments.

Such experience will be critical. Because I believe addressing climate change will be impossible without a new international climate agency: an organisation with the power to lay down and enforce terms on national governments.

Pursuing the four energy principles I have talked about this evening – forging a cross-border approach; improving data; promoting technology deployment; and providing global leadership – will be impossible without collaboration.

Business, scientists, and NGOs will all play a crucial role.

However, I believe we are facing an energy and environmental challenge as great as *any* challenge mankind has faced.

And at times like this we look to governments, to our elected officials and public servants, for leadership.

Jean Monnet, one of the founding fathers of the European Union, said that his main objective in life was, and I quote:

“To make men work together, to show them that beyond their differences and geographical boundaries there lies a common interest.”

It is my sincere hope that our current generation of leaders take heed of these words.

Thank you very much.

Lord Browne of Madingley

7^h May 2008