CBI
THE VOICE OF BUSINESS

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Worshipful Company of Fuellers Annual Lecture 2011

‘Is UK energy policy fit for purpose?’

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-----CHECK AGAINST DELIVERY-----

Master of the Worshipful Company of Fuellers, distinguished guests.

I'm delighted to be with you this evening, and in such magnificent surroundings.

Some you may know that this wasn't the first Draper's Hall on this site. A previous incarnation was destroyed in the Great Fire of London.

And there's a connection here with the Fuellers, not because they caused the fire, I might add - Thomas Farriner, a baker just around the corner on Pudding Lane, was to blame.

But a predecessor company, the Livery Company of Woodmongers and Coal Sellers, handled most of the monies used to rebuild the City after the fire.

I'm afraid to say that the new Drapers' Hall was hit by fire again a hundred years later and rebuilt a further time. There have been alterations since, but it's been fire free and, touch wood, we'll get through tonight unsinged.

But enough of 1666 and all that. My job isn't to talk about whether the smoke alarms are fit for purpose, but rather whether the UK's energy policy is.

There's no other issue more important to business, and no other area where striking the right balance is more challenging.

Meeting the needs of suppliers and users and protecting the environment isn't straightforward at the best of times.

Add to that some patchy past government policy, and it can make you want a lie-down in a darkened room.

But groups with different agendas can come together for common purpose. The membership of the Fuellers' Company demonstrates that.

In this room are representatives from the coal, oil, nuclear, gas, electricity and renewable energy industries – and from all parts of them, from production and distribution to research, marketing and finance.

The answer might be to lock the doors and not come out until we've agreed a way forward, assuming the wine supply holds out.

But let me give the overriding business message: we cannot build a lasting economic recovery if we do not have a secure, reliable and affordable energy supply.

And business wants equally to play a leading role in meeting the low-carbon challenge.

The future of the UK energy system is fundamentally a story about investment. We all know that to make a return, you have to take risks. There are market risks, there are technology risks, there are construction risks. And of course, there are policy risks. There are few other industries where policy risk is more likely to keep potential investors awake at night, and consequently to keep their wallets in their pockets. As things stand, the energy policy landscape won't solve this problem, so it won't deliver the investment we need. The CBI and its members have been saying this since 2009. And the government has heeded this warning. In the electricity market reform White Paper in May, it took some positive first steps towards addressing the issues.

But the whole picture is still one fraught with unanswered questions and risks. Until we answer those questions and mitigate those risks, investors cannot make decisions and the necessary investment will not flow.

We know the capital is available. But as things stand, some investors are not yet seeing the UK as an attractive destination for it.

So what more do we need the government to do?

On the positive side, the government is putting some of the right building blocks in place.

If implemented correctly, contracts for difference will provide certainty for investors by creating a stable price for electricity generated from renewables, carbon capture and storage and new nuclear.

On balance, CBI members supported this over the Premium Feed-In Tariff, but there are issues which need to be ironed out.

We need to know what the reference price and the strike price will be for each technology. Get those wrong and we'll all end up paying too much for new technologies. And in setting those prices, the government will need to be aware of – and mitigate the potential for – information asymmetry.

You'll know better than me that Whitehall isn't always great at commercial negotiation. The government will need to up its game and set rates that are appropriate.

But before we even get to contracts for difference, we'll be under the renewable obligation regime for five more years. We need to know what those five years are going to be like.

The government has been promising us a consultation on the future of the obligation since the start of the summer.

We think there should be two priorities for it: one, it should incentivise the deployment of the most cost-effective technologies; two, it should encourage the development of technologies where the UK can build a competitive advantage and be a world leader.

While we're doing all of this, we need to keep the lights on. To do that, the government believes we need a capacity mechanism, but has not yet defined quite what. We need certainty from the technical update that's due at the end of the year as to whether it will be a strategic reserve or a market-wide mechanism. And we need to be involved in that decision-making process.

We also need to know what's happening with carbon capture and storage. The first announcement of a competition to develop this was made almost four years ago, back in November 2007. We still haven't had the announcement of a winner. As a result we've seen companies announcing their withdrawal from the contest.

The common thread though all of this is that the government can get this right if it talks to the experts – like the ones in this room.

In 2001, the New Electricity Trading Arrangements were introduced. The process leading up to this involved the government listening and talking to the industry.

That was a sensible approach. I'm not saying we should use that exact model again – but we need to find a way to have a conversation.

But there are some areas where the government has already missed its chance to talk to industry.

The North Sea oil and gas tax, the changes to solar feed-in tariffs, the carbon floor price and the removal of the revenue-recycling element of the carbon reduction commitment all came with little or no consultation, warning or heed for investors.

The North Sea tax has increased investor concern about the potential risk of investing in the UK as a whole – as well as undermining the case for continuing investment in North Sea production.

As for the solar feed-in tariff, it's only right that the government reviews and adjusts incentives so as to keep them effective and fair for everyone. But moving the goalposts with little warning doesn't just upset those investors directly affected. It also creates a worrying climate of uncertainty for every business considering investing in the UK.

We need to show the world that the UK has a stable policy environment and a consensual policy-making process if we're to secure the hundreds of billions of inward investment required over the coming decades.

On the carbon floor price, which was announced in the Budget in March, I'm concerned that the most immediate risk for the government is that we're in serious danger of jeopardising our energy-intensive industries.

In providing a unilateral floor price to give investors certainty for investment – especially in nuclear power, which the CBI recognises the need for – we have damaged the international competitiveness of key manufacturing sectors vital to exports and to the rebalancing of the UK economy.

This will hamper the recovery and do nothing to reduce global carbon emissions. And yet this is what current policy would do – and it would be a spectacular own goal.

We have persuaded the government to mitigate the impact on most affected areas - its forthcoming plan for the energy-intensive industries has to create an immediate solution that protects them while keeping the ambition going on electricity market reform and emissions reduction.

Energy-intensive industries underpin the UK's manufacturing, making products as diverse as the steel and chemicals needed for wind turbines; low-rolling resistance tyres; strong and lightweight aluminium; and the bricks, glass, tiles and insulation needed in new buildings. Global demand is growing for these materials.

Success for these firms means success for their supply chains, meaning a large multiplier effect on economic growth and jobs.

We need to show the world that the UK can continue to be a manufacturing powerhouse at the same time as cutting emissions. A key part of this is maintaining the competitiveness of energy-intensive industries.

We've proposed a rebate-based exemption from the carbon floor price linked to the industries' work on energy efficiency. They need to pull their weight, and to reduce their emissions. They want to – and many already are. They don't want their fuel bills to be any higher than they need to be. So we should help them use renewable heat, energy from waste and more of the other innovations out there.

Achieving this will require a working, flexible and future-proof exemption model, and that's not going to be as simple as we'd like.

It's going to be impossible for energy suppliers to work out the rebate themselves. It's just too complicated to put on their bills. So our proposal is a rebate based on a weighted average energy mix.

It may require a different level of rebate for different sectors. That's why a clear definition of energy intensives is so important: businesses need to receive rebates when they qualify as a risk, so that everything's transparent.

So that's energy intensives.

The next important thing is the cost for average energy users. Small businesses and domestic customers are seeing their bills go up before any of the EMR changes have occurred. While this can't be helped, that doesn't stop it hurting and it's a big part of the reason we're calling for changes.

The Carbon Reduction Commitment was meant to be green, aimed at encouraging energy efficiency in business by recycling financial incentives. Late last year business lost the incentive payment as a contribution to balancing the government's books. Now it's just a cost and a complex scheme. If the government wants a green tax to encourage energy efficiency, it should do the job in a more straightforward way.

Businesses are currently facing three different carbon taxes: the climate change levy; the CRC; and the carbon price floor. They could also be facing two different reporting requirements: the CRC league table and mandatory carbon reporting under the Climate Change Act.

This needs to be simplified. Why can't we have one tax, and one reporting requirement? Maybe then, the policy landscape could achieve what it's meant to – incentivise energy efficiency.

This is the other side of the coin of the electricity market reform debate. We need to think about what we're doing to help companies that want to invest in this country save energy.

We also need to think carefully about this from the perspective of the consumer.

There's a huge amount of energy efficiency potential in our built environment that's not exploited properly. We need a much more coherent approach to saving energy across the economy, because we know the best and cheapest way to supply energy and reduce emissions is to become more efficient.

We also need the government to ensure it's doing all it can to help people save energy, and to articulate the potential we see in projects like the Green Deal. We've not done enough to sell the benefits of changing our energy use, and of going low-carbon.

Right now, 75 per cent of people don't think about energy efficiency when they buy a home.

When we present the Green Deal, we shouldn't be talking about targets we have to hit. We should be selling its benefits. The people who will deliver it – the people who will finance it, or who will be putting in the insulation and the double glazing – know the potential for this scheme, but they're worried we're not exciting the public enough to get them to take it up.

If people just see the government's approach to energy and tackling climate change as yet another cost to be shouldered, then we won't achieve our aims.

I've spoken about two of the pieces of the puzzle we have to solve if we're to decarbonise our economy and help deliver growth.

We have to get EMR right, and to improve on the mistakes of the past when business wasn't consulted. The government needs to talk to industry to get the details right on contracts for difference, on the renewables obligation and on the capacity mechanism.

We have also to become much more energy efficient. That's about providing industry with simple incentives, not ever-more complicated tax and regulatory regimes. And it's about selling the benefits of energy efficiency to consumers.

There's a third piece of the puzzle.

We need to redouble our efforts to get international action on carbon. In the absence of sufficient commensurate commitment, we're now taking unilateral action in the UK to embed the price of carbon, putting our actions far out in front of our EU counterparts and any international economies. We should be one step ahead in order to provide leadership, but we're not much of a leader if we don't have any followers.

For this reason, we need to press for an ambitious international agenda, and to see Durban begin to achieve what Copenhagen failed to. That's why the CBI is hosting a dinner next month with Christiana Figueres, the Executive Secretary of the United Nations Framework Convention on Climate Change - to make clear how critical this still is to business.

That's my final thought. We need a global deal so that all the effort we're putting in to energy in this country isn't wasted, and so that the UK can be at very front of the economies of the future.

We can and must get this right.

It just remains for me to thank the Worshipful Company of Fuellers for allowing me the opportunity to speak to you this evening, and to wish you all well in meeting the challenges ahead.

Thank you very much.

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