

What does the new Government mean for energy and climate change?

17th December 2019



Now the UK election is over and the new Government has been formed, what are the implications for energy and climate change?

Key points:

- With the Conservative Government re-elected with a large majority, the much delayed Energy White Paper is now expected in the first half of 2020.
- However, this may well fall short of a comprehensive plan on how the UK reaches its legally-binding Net Zero target by 2050.
- The pressure on the Government to come up with such a plan will grow through 2020 as we approach the COP26 climate summit in Glasgow in November 2020.
- Meanwhile, the EU27 have also now signed up to a Net Zero target by 2050, and committed at least 25% of the EU's long-term budget to climate action in its 'Green Deal'.

Net Zero a top priority

Following his success in the general election on 12th December, Boris Johnson confirmed that his Government would put the UK on course to reach net zero emissions by 2050, identify this as one of his six "guarantees".

A major reshuffle, including potentially the re-creation of a dedicated department to tackle climate change, is expected in February, once the UK leaves the EU. For now, Andrea Leadsom continues as Secretary of State for Business Energy and Industrial Strategy (BEIS), with Kwasi Kwarteng as the Energy Minister. This will provide a good deal of continuity in the broad direction of travel on energy and climate policy.

While Brexit will still dominate the work of the Government, the UK is hosting the COP26 Conference in Glasgow in November 2020. This will increase pressure on the Government to have a coherent plan on how to meet its legally-binding targets for emissions reduction.

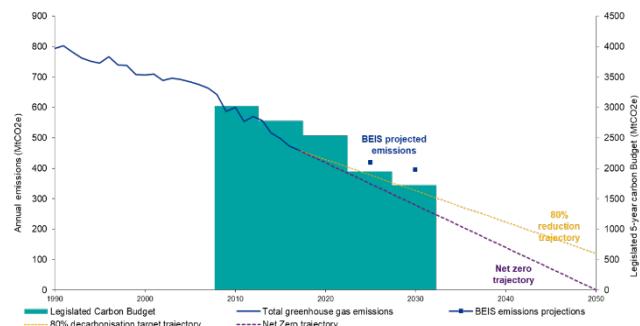
1. Energy White Paper

The Energy White Paper was originally drafted and ready to go back in July. But it then got delayed due to the change of Prime Minister, and was delayed again because of Brexit. It is now expected to emerge in the first half of 2020. Previously, the Government indicated that this would be followed by a 'Heat Strategy' in the summer of 2020. It is not yet clear if these two documents will now be brought together into one single plan for achieving Net Zero, or continue to be published separately.

Either way, the Government is going to have to start putting in place the policies to drive faster decarbonisation across all sectors of the economy than is currently the case. As laid out below, the latest published

projections show the UK missing the 4th and 5th Carbon Budgets, covering the period up to 2032. As the Climate Change Committee has noted, radical and swift action is now needed if the UK is to meet its targets and minimise the costs of this transition.

Carbon Budgets and Net Zero target to 2050



Source: BEIS, KPMG analysis

Based on the consultations issued previously and the commitments in the Conservative Party Manifesto and those made during the election campaign, we expect the following policy issues to feature prominently in the forthcoming White Paper:

2. Retail price cap to continue

A market-wide retail price cap was introduced in 2018. This was intended to be a temporary measure designed to protect consumers whilst other reforms to stimulate competition were implemented. Since then, we have seen dramatic changes in the retail market, with about 20 small suppliers exiting the market, or being taken over since early 2018; the Npower/Eon merger leading to widespread job losses; and Ovo taking over SSE's domestic retail arm. As a result of these changes, the former "Big Six" suppliers will service just over half of

of the retail market, down from over 90% in 2010⁽¹⁾. Newer entrants are not yet making profits. Despite this, the price cap seems set to stay, with every prospect of it being extended at least until 2023, the final year under the current legislation.

3. £9.2bn for energy-efficiency

The Manifesto promises an extra £9.2bn of public spending on energy-efficiency measures in homes, schools and other public buildings to “help lower energy bills”. This comes on the back of significant cuts in spending on energy efficiency in recent years, with total spending now about 1/3 of the level it was back in 2010. The White Paper will have to set out how this money is to be spent and over what period. Presumably, it will involve some targeting on the fuel poor. But the details have yet to emerge, including on how it would work with the current ECO3 obligations.

4. £800m for Carbon Capture Utilisation and Storage(CCUS)

In a similar vein, the Manifesto announced a big spending commitment (£800m) to “build the first fully deployed carbon capture storage cluster by the mid 2020s”. This comes after two failed competitions for CCS on power generation and the withdrawal of £1bn of capital funding for CCS that previously existed in the early years of the Coalition Government.

The focus this time appears to be on CCUS and industrial clusters. The funding will go to develop one such cluster, presumably after some sort of competition, or process to down select the various clusters that might wish to put themselves forward, including Humber and Teesside.

The White Paper will need to clarify next steps on this as well as what other policy steps are being taken to incentivise the use of CCUS.

5. 40GW of offshore wind by 2030

A surprise during the election campaign was the Prime Minister's announcement that the target for offshore wind deployment, agreed with the industry only earlier this year in the Sector Deal (30GW by 2030), was being increased to 40GW.

This will test the supply chain's ability to ramp up, particularly post-Brexit. BEIS may also need to review the frequency of CfD auctions, as well as provide some clarity about what happens after the next two auctions (2021 and 2023) if the industry is to deliver this goal.

Looking longer term, the CCC have recommended 75GW by 2050. With offshore wind now effectively “subsidy free”, it seems that this technology will be deployed at scale around the UK as part of the move to Net Zero.

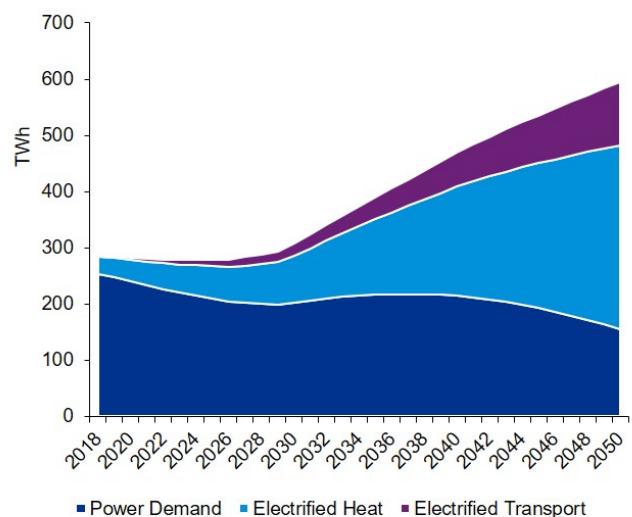
6. Regulatory Asset Base (RAB) funding model for new nuclear

The Conservative and Labour Manifestos both referred to “supporting” nuclear, without giving any further details on what that support would entail.

For the Government, the role of nuclear stems from the volume of low carbon electricity needed in a Net Zero economy. With high levels of electrification of transport and heat, we could see a doubling of power demand by 2050 (see chart below).

Source: (1) Ofgem

Power Demand Projection



Source: National Grid FES

The White Paper will need to provide a clear statement on the use the Regulated Asset Base (RAB) model for new nuclear and next steps to bring this about.

It will also need to clarify whether Small Modular Reactors (SMRs) also have a place alongside large-scale nuclear reactors in the future energy mix.

7. Moratorium on fracking

The Manifesto commits to a “moratorium on fracking with immediate effect”. This represents major U-turn for a Government that was pushing fracking hard only a few years ago as the solution to Britain's energy needs.

8. Support for electric vehicle (EV) charging infrastructure

The Government is committed to investing £600m over a six-year period to support new EV charging infrastructure to reduce range anxiety and kick-start the shift to EV.

The White Paper will need to explain how this money will be spent and where those charge points will be built.

9. Doubling of international climate finance

The Government says it has doubled International Climate Finance. It says it will use the forthcoming COP26 Conference to ask our global partners to match the UK's ambition.

10. New climate risk reporting requirements

The Task-force on climate-related disclosures (TCFD) framework, requiring companies to report on their risk management, strategy, governance and metrics in respect of Climate Change, are expected to become mandatory for all UK listed companies in 2022. Mark Carney's appointment as Special Envoy to the UN on Climate Change and Finance could herald moves for earlier adoption of global standards on climate risk. This may be one area where progress could be made at COP26.

11. £4bn of new funding for flood defences

In recognition that climate change is happening already, the Government has said that it will spend an extra £4bn on flood defence in the coming years.

12. System operation

The final reports on the 9 August power cuts are due out shortly. We expect all parties involved (National Grid, power generators, the Distribution Network Operators and the Train Operating Companies) to attract some criticism and have recommendations to implement. This may also reignite the debate about the future governance of power system operation in the UK. Before the election, Conservative Ministers seemed to indicate their support for moving to a fully 'Independent System Operator' (ISO), like those that operate in some US states. This could also feature in the forthcoming White Paper.

The EU 'Green Deal'

The UK may be about to leave the EU, but what the EU does on energy and climate is still hugely important to the UK and the world. Last week, EU leaders signed up the remaining 27 countries to meet Net Zero emissions by 2050, thus bringing the whole of the EU in line with the commitment made by the UK and France back in June. The EU also agreed tougher cuts in emissions by 2030, expansion of the EU Emissions Trading Scheme to cover new sectors, reforms to energy taxation, big increases in spending on climate change and a possible Border Adjustment Tax to limit the risk of carbon leakage.

Brexit and energy

With a Conservative majority, it now seems very likely that the UK will leave the European Union on 31st January 2020.

In energy terms, under the current deal, electricity and gas is still expected to flow through the interconnectors post-Brexit. However, there may be impacts on trading positions through changing macroeconomic conditions, including exchange rate movements.

Perhaps more important is how attractive the UK is seen as a place to invest post-Brexit and, like other sectors, the impacts on supply chains and the availability of skilled labour.

Energy has the largest infrastructure needs of any sector of the economy and foreign capital is key to ensuring that Britain has the energy infrastructure and supplies it needs.

Conclusion – All roads lead to Glasgow...



Photo source: BBC

Location: Scottish Event Centre, Glasgow, Scotland, UK

Date: Monday 9 November 2020 – Thursday 19 November 2020

The UK will host the COP26 climate summit in Glasgow next November. This will come just days after the result of the 2020 US Presidential election.

According to the UNFCCC, we are entering the last decade when effects of climate change can't be kept to a manageable level. The cuts agreed at the Paris Conference in 2015 came into effect in 2020 and progress on national plans is due to be reviewed at COP26. So COP26 will be a key moment for the UK and the world.

The UK Government will therefore be under intense political pressure and international scrutiny to come up with a convincing plan ahead of COP26 on how to get to net zero emissions by 2050. Some of the elements of this plan, like a big expansion in offshore wind and take-up of electric vehicles are starting to fall into place. But much remains to be done over the next few months if a clear, comprehensive plan is to emerge in time to present to the world in Glasgow.

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