

Speech given by Dr Paul Golby, Chief Executive, E.ON UK at the BIEE Conference on Wednesday, 22 September 2010

“Energy in a low carbon economy: New roles for governments and markets”

Good morning.

I'm delighted to have been asked to speak to you today. Prior to a pretty hectic period for industry and policymakers, it's useful to have the opportunity to take stock and discuss the challenges ahead for our industry.

As well as speaking to the theme of the conference and considering the relationship between Governments and Investors, I also want to cast a light across the energy landscape as a whole.

Too often in recent years, I've found myself on conference platforms and found we've focused solely on one area of our industry, as if the rest of it was either someone else's responsibility or we didn't have to worry, it would take care of itself.

Put another way, at times you might have been forgiven for thinking that Energy CEOs and their plans to build power stations were *all* that mattered, such has been the focus on upstream issues.

As to today's title, for me there's word missing.

It's "customers".

Otherwise we're like a group of English students discussing Hamlet without mentioning the Prince...it misses the point.

The real challenge of our time is not just whether this or that power station goes ahead. It's actually whether we can develop a truly low carbon energy *system* that meets the needs of our society, our economy and our planet.

That means decisions upstream on nuclear and CCS, yes, but it also means equally far-reaching changes to our make our networks smarter in midstream and addressing the scandalous energy inefficiency of our homes and businesses.

Two years ago, we helped frame the debate upstream when we started talking about "the trilemma" – how we provide affordable, reliable and low carbon energy for our future.

Not before time, we now need to widen the scope of what we mean. It can't only be about the big decisions on generation - it has to be root and branch reform to all aspects of our industry.

Restating the trilemma

There's obviously been a significant level of political change over the spring and summer.

We have a new Coalition Government that has spelled out at a high-level its energy policy priorities. Perhaps understandably there has been a lot of media interest in the views of the new Secretary of State, particularly on new nuclear.

While this interest is understandable, I'd rather focus on the policies than the personalities and for the record, the Coalition Agreement published in May is a good basis for moving forward. But as ever, the devil will be in the detail.

And there is much more work to do...and, as we know, less money than ever in the coffers to do it with...all at time when the way energy is produced and used is changing as we move towards a low carbon future.

So let me start with the first of the big issues on the Coalition's agenda – Electricity Market Reform.

Upstream

To get into this, it's probably worth setting out some of the key points that underpin our view of the future.

We expect that electricity will eventually replace the direct use of fossil fuels for both domestic heating and for transport, through electric cars.

Like most people, we think the upstream energy mix will be principally based around new nuclear power, more offshore wind and the development of carbon capture and storage to allow us to continue to burn fossil fuels into the future to give us system flexibility. This will ensure we have a low carbon energy supply that is also reliable and affordable.

So far, so familiar then.

Something else that will be familiar to you is that our current energy market is not fit for purpose. As someone who famously (indeed *infamously* in some quarters) said "the market is bust" some years ago", it's like having déjà vu all over again.

And believe me, the clock is ticking...and despite what the Secretary of State said in his recent evidence to the DECC select committee, a carbon floor price alone will not be sufficient. You can't build a power station by reinforcing the floor only.

The recession has bought us a couple of years at most but the decisions pending are of critical importance and do need addressing soon.

So the priority now is to agree a coherent energy policy framework that will incentivise the investment required, circa £200m, and make the UK an attractive place to invest.

The UK has set ambitious goals for low carbon energy and this Government (and in fairness, its predecessor as well) has recognised these will simply not be met without reform of our energy markets.

The Government will be consulting this autumn on its preferred option from those set out in the Energy Market Assessment published with the April Budget.

At a high-level, what is needed from this process is clarity:

- Clarity from business on what it needs in order to invest and
- Clarity from the Government

So let me be clear!

I would argue that clarity is best delivered by a mechanism that is robust and established for the long-term, one that is immune (so far as is practical) from short-term political interventions. It's for those and other reasons, that I am sceptical about the merits of a tax to underpin the carbon price. Investors are not going to commit multi-billion investments on the basis of the level a tax might be set at by the Government of the day in the 2020s or 2030s, which is the timescale which will be relevant to the long lead time investments we are making over the next few years.

Instead, having looked at the options we would support the introduction of a Low Carbon Obligation (LCO). Working in a similar fashion to the RO, this would provide a more reliable source of revenue than a carbon tax, would be less subject to political uncertainty than a tax and would be more effective in underpinning essential long-term investments such as nuclear.

We also believe that an LCO would be for more consistent with ensuring that the UK energy market retains the discipline and rigour that competition and markets provide – both unfashionable words perhaps but in my view important ones. In other words, as well as its other merits, I believe it will be more efficient – delivering the investment the industry needs without the risk of the customer paying too much. The UK Government has consistently been arguing for more competition in the rest of Europe for the last twenty years. It would be ironic if, having made real progress in delivering that objective, we now turn our back on competition.

There are no easy answers here. That's why we need the Government to recognise that there are a number of options on the table which need to be properly considered.

A hasty consultation where the outcome is already prejudged would be the worst thing this Government could do to undermine investor confidence and would create the impression that it was developing policy to suit the loudest voice in the room.

I'm interested in hearing your thoughts today on this.

Midstream

As I argued a moment ago, changes in how we use and produce energy have implications right across the UK's energy system. In some respects, nowhere are these challenges more acute than in our electricity networks, the importance and scale of which has been overlooked for too long.

Electrification of heating and transport and the growth of decentralised energy generation are a challenge, sure.

But they are also an *opportunity*: to take today's passive, one way system and turn it into an active, two-way "smart grid".

The pressure to do so is two-fold.

It comes first, from the major investment upstream in new nuclear, offshore wind and cleaner fossil fuels – much of which will be located near the coast - that must be securely and reliably connected up.

Secondly, we know we will see major changes in how customers use energy in their homes as well as to travel.

If you add to that agenda the pace and scale of the anticipated roll-out of smart meters then it's clear change is needed to the 'glue' that binds the system together – the electricity network.

A smarter network will help the network companies manage more effectively the extra peaks and troughs in demand that an increasingly decentralised energy world will bring, helping to minimise overall network investment costs.

And as we do so, we will improve the experience of all energy users as we bring the networks into the customer age.

Ofgem does not often get plaudits for forward thinking from stages such as this, but on this occasion we should acknowledge the key role their Low Carbon Networks Fund will play.

My distribution business, Central Networks, has recently submitted a bid to this fund to support a flagship project in Milton Keynes called "MKSmart2020". Working in partnership with Milton Keynes through their Low Carbon Living Programme, Central Networks wants to develop Milton Keynes into a fully functioning low carbon network, a working microcosm of urban Britain in 2020 based around:

- Twenty thousand smart meters and in-home displays across the area
- Collaboration with the local authority and the Open University on understanding the best way of communicating with householders as they commence their own energy efficiency journey
- Creating between fifty to sixty new “smart homes” built around smart appliances and charging points for electric vehicles. The project will also look more widely at how we can integrate the infrastructure needed to support the increase in electric vehicles I mentioned a moment ago.

This is an exciting project, one that could give us all the opportunity to learn about 2020 networks and how they will need to evolve to meet the demands of a low carbon energy system and just as importantly, how people interact with these technologies.

The bid, which has widespread support across Milton Keynes, is a strong one that would deliver real benefits for the UK as a whole as the lessons we learn would be rolled out and applied elsewhere.

I don't think we should underestimate the potential here – not least for customers.

As we know, it wasn't the doctors but the engineers who drastically improved public health in the nineteenth century. Surely, it will be in no small measure the network companies who will help deliver our low carbon future.

Downstream

Our Milton Keynes project is about how to best develop the network to support consumers and help them change their relationship with the energy they use in their everyday lives. It is one part of a bigger challenge facing our industry which is to think differently about energy from both sides of the meter. Nowhere is the need to do this more pressing than in our homes.

But first a question for you:

“Why on earth would an energy company want you to use less energy?”

Hopefully, you'll recognise the question from our current advertising campaign. It goes right to the heart of the relationship between energy supplier and customer and seeks to tackle head on the issue of trust (or lack of it) between the two.

It is a sad fact that customer trust in all energy companies is poor and not at all where it should be.

This is a particular concern to me as we'll have to ask so much of our customers over the coming years – to improve the energy efficiency of their homes, to change the way they use energy, and to allow us to build the generation assets this country needs. Because, ultimately, we'll be asking them to support this investment through their energy bills. We need to make sure that our customers trust us – politicians and energy companies alike – to make the right decisions.

Improving the relationship between the industry and the customer is the first step and we know we must do more. But actions speak louder than words, and we also know we need to back that up with products and services that help the individual customer in their own home or business.

So, in the same way that people have become accustomed in the home and at work to think “reduce, re-use and recycle” we need a similar focus to support customers as our relationship changes.

I’ve been trying to think of a way in which we can best describe the scale and scope of the change that is about to happen to our industry.

Simply put, technology changes that lead to social change are *always* underestimated. To me it’s clear. Micro-generation is not a photo opportunity for Prime Minister’s past and present. It’s a fundamental part of our low carbon future. Times are changing and so is my business. Customers are ceasing to be just a meter point but are becoming active players in the market. The advent of Smart technology will put more information and knowledge in the hands of the consumer and this will give them more control – over how they use energy, how they produce it and who they choose to trade with.

In the future, in addition to supplying energy, an energy company’s relationship with its customers will revolve around how we help them:

1. insulate their homes
2. moderate their energy use,
3. generate their own energy

Increasingly we will be working in partnership with communities as well as the individual customer. Why? Because as well as the difference we can make in people’s homes, we can also see the potential for changes across neighbourhoods and communities as well.

I cannot say more about this at the moment but look out for these partnership announcements in the weeks and months ahead.

Implications for Government and Investors

I've talked a lot this morning about what's happening across the energy system as we prepare to accelerate the transition to a low carbon economy. I'd like to close with a four key points about what this all means for Government and Investors.

The first point I would make here is something I've long called for – a roadmap.

I don't doubt for a second the urgency in delivering a low carbon economy. But there is a very real danger that without a shared understanding among policymakers, investors and consumers about what the ultimate destination is we will simply ending up pulling in different directions. We can't repeat the mistakes of the past which has too often involved setting up arguments that lead to piecemeal, sticking-plaster decisions about different technologies.

The Government needs to set out a clear sense of direction of how it sees the UK's 2030 and 2050 goals being met.

Second, and to emphasise a point I made earlier, reform of electricity markets should be about doing just that – *reforming* markets, not *abandoning* them.

So on this occasion, I was pleased to see the Secretary of State's comments on the floor of the House of Commons last Thursday in response to a question about creating low carbon incentives when he confirmed "I am a great believer in the virtues of the market..."

Yes, we know the current system is not fit for purpose but we will not get far in encouraging investment on the scale we need by washing our hands of competition and markets and handing these decisions back entirely to the State.

Third, stability – for us and the customer.

Nothing is more damaging to investment than uncertainty (such as CCC with CCS on gas post 2020). As a major investor we need to know what the framework is and not have it changing - or being threatened with change - every five minutes because of a new piece of modelling. Whilst we accept that policy does need to be reviewed from time to time, this should be kept to a minimum and existing investments protected.

We should not forget that customers also need stability in their incentives – this is not their business and the changes may seem scary at first. It's why mechanisms like the feed-in tariff and the renewable heat incentive can help incentivise homeowners to adopt low carbon technologies – so long as consumers feel that they can have trust in them and that they are not about to disappear.

Thank you for listening. I look forward to your questions.

ENDS