

**Rt Hon Edward Davey MP**

Secretary of State for Energy and Climate Change

**Speech: Energy Divided? Building Stability in Energy Policy**

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**AS DELIVERED**

**INTRODUCTION**

It's a great pleasure to be here at the IPPR.

Since your formation in 1988, you have been at the heart of progressive policy making.

Now in 2014, with the old, rigid, two party political system breaking down, organisations like IPPR have new opportunities to reinvigorate political thinking.

It allows you to take risks and break orthodoxy rather than simply being seen as the policy unit of a particular political party.

Your work on climate change and energy markets is a good example of this – a key part of your work for which we are very grateful.

Your 2012 investigation into the costs of energy has been influential, not only on government legislation but informing the work of the regulator Ofgem too.

**ENERGY DIVIDED?**

The title of my speech today is Energy Divided? Building Stability in Energy Policy.

And I want to talk about the challenges of setting out long-term policy frameworks in the context of multi-party democracy.

Frameworks designed to bring lasting transformational change to society.

The sort of change we need if we are to power our homes and businesses in a way that addresses climate change – and crucially – meet the social needs of our citizens for secure, affordable energy at the same time.

Frameworks like the 2008 Climate Change Act that set Britain on the path to a low-carbon society by the middle of this century.

Frameworks like the 2013 Energy Act that puts in place the long-term financial and legal mechanisms in energy required to meet the ambitions of the Climate Change Act.

Both of these Acts passed through Parliament, under different governments, with wide cross-party support.

So all political parties in Britain can take credit for the transformational power of government in this regard.

Over the next decade we need to see tens of billions of pounds of investment in new clean energy generation and networks if we are to replace the old and dirty infrastructure that is set to close.

And this needs to be pre-dominantly low-carbon, reliant on new and maturing technologies that are currently more expensive than established fossil fuels, especially as fossil fuels don't yet pay the full cost of their climate pollution.

So this throws up two challenges for political parties.

First, investment.

If we are to persuade companies to make long term investments in Britain's low carbon future, they need to see that there is a political consensus on energy and climate change policy that rises above the normal everyday partisan politics.

That politicians are ready to put the national interest above party interest.

Second, the public.

If we are to bring our people with us on this journey, we need to demonstrate that we will both protect the planet and power the country in the most cost-effective way possible.

To show that going green will bring jobs and grow the economy too.

Making people's lives better and not costing the earth.

Part of this is demonstrating that throughout this process, we will look after the poorest in society and keep energy bills as low as possible for everyone.

So far, by passing the 2008 Climate Change Act and the 2013 Energy Act with cross-party consensus, British political parties have risen to these challenges.

And today I will set out for you how we are progressing thanks to these frameworks – as we are progressing far faster and far more than many people realise.

But first – I have to sound a warning.

For I fear that the political consensus on energy and climate change that's been so crucial in making progress to date is in danger of breaking down.

## **FROM THE RIGHT**

From the right, fringes of the Conservative Party and UKIP are parroting the arguments of the most discredited climate change deniers.

Seizing on any anomaly in the climate data to attempt to discredit the whole.

This is undermining public trust in the scientific evidence for climate change – which is of course overwhelming.

And we can see around us today the possible consequences of a world in which extreme weather events are much more likely.

This type of climate change denying conservatism is wilfully ignorant, head in the sand, nimbyist conservatism.

And when married to the europhobia innate to parts of the Conservative party, you have a diabolical cocktail that threatens the whole long-term structure of UK climate change and energy policy.

If you accept the logic of climate change, you have to accept the logic of European co-operation to tackle it.

Because we can only remain competitive, be energy secure, and tackle emissions by acting together with our major trading bloc – our neighbours – our partners.

And we can only influence the world's biggest carbon emitters – China and the USA – by speaking together as one.

The European framework isn't perfect; I'm the first to admit that.

That is why the UK has been playing a leading reforming role in Europe as we put together the new 2030 energy and climate change framework.

It's why last year I set up a new like-minded group in Europe – my Green Growth Group – where now 15 member states are working together for an ambitious, practical European agreement to cover the next 15 years.

I have been working hard with my fellow European ministers to reform the emissions trading system;

To complete and liberalise the single energy market;

To better connect Europe together - with energy networks that can help us trade electricity and gas so we bring down prices and increase liquidity, diversity and security;

And, above all, to make sure collectively we remain ambitious on cutting greenhouse gases.

So in Government, the Liberal Democrats have been demonstrating that active engagement with our European friends is possible, is in the national interest and can bring results in areas as crucial to our future as energy and climate change.

I have been supported in this not just by Nick Clegg and my Liberal Democrat colleagues but by many Conservatives too.

And I want to pay tribute to the work of my ministerial colleagues, Greg Barker, Michael Fallon and Baroness Verma in this regard.

But I would fear for the future of the integrity of the Climate Change Act and the Energy Act if an extremist cohort found themselves in a position of real influence after the next election.

### **FROM THE LEFT**

But this is not the only danger to the political consensus on energy and climate change.

The other difficulty is more subtle – and challenges all parts of the political spectrum.

And it lies in the role of the state.

How government resolves the well-known tensions in energy policy – the so called ‘energy trilemma’.

Meeting the requirements of decarbonisation, security and affordability at the same time.

To do this we are acting to put in place the regulations, markets and financial instruments to encourage the investment we need to go green and keep the lights on – but in the most cost-effective way.

This is very much about an active state.

The 2013 Energy Act represents a carefully judged state-led market intervention that diminishes overtime as low-carbon power generation reaches grid parity in a future electricity market where carbon is properly priced.

But the balance is delicate.

And where I see future problems is in misjudging the realities of the energy trilemma and seeking the wrong strategic balance between the market and the state.

Either too much or too little state.

Too much or too little market.

And this is what concerns me most about Labour’s approach.

I believe Ed Miliband misjudged this balance in his party conference pledge to artificially hold down energy bills, regardless of the consequences.

Labour's energy bill proposal is based on a false analysis of the market.

It will, in fact, threaten investment in energy security.

Push up prices for consumers in the long-run.

Destroy competition by solidifying the power of the Big 6.

And do nothing at all to reduce emissions.

Indeed, if it threatens investment in low-carbon generation, it could represent a step back for the climate.

And Labour have failed to recognise how carefully the Coalition has approached this balance of market and state.

What we have been doing to bring on essential low carbon investment.

What we have been doing to address the problems in energy markets they created so Britain's energy firms have to deliver a better deal for consumers in the future.

For our record is one of substantial green growth and more competition.

Let me start with the investment picture.

### **INVESTMENT IN LOW CARBON ENERGY SECURITY**

Today, 40% of our electricity comes from coal.

20% is from old nuclear.

Most of that is due to come off line in the next decade.

So the Coalition Government inherited a massive investment challenge - the result of under-investment over many years.

Official statistics suggest that, in the ten years to up to 2010, investment across the whole of the electricity sector totalled around £30 billion.

An average of just £3bn a year.

The Coalition has been working to turn this around.

Latest DECC estimates suggest that around £40 billion has been invested in new electricity infrastructure since 2010 - overhauling the record under the last administration in just over 3 years.

Labour's recent Energy White Paper, citing Bloomberg's New Energy Finance 2013, claims that energy investment in renewables has been falling since 2009 to under £2bn in 2013.

But that's simply not true.

In fact, Bloomberg's figures show, average annual investment in renewables in this Parliament has more than doubled, with renewables investment in 2013 at record levels.

On Bloomberg's measure, between 2005 and 2009 renewables investment averaged just over £3bn a year.

But since 2010, it has ballooned to almost £7bn a year, with 2013 showing a record high of almost £8bn – higher than at any time under the last Government.

But because of the historic under-investment, we still need up to £110bn of investment in electricity generation before the end of the decade, much of it in renewables and low carbon generation.

The stable regime we have put in place under our new Energy Act is creating the world's first low carbon electricity market.

It has the potential to unlock additional investments up to 2020 of at least £40 billion in renewable electricity generation projects alone.

I recognise this barrage of statistics can be confusing – and here I have only touched on electricity generation and renewables investment.

There's much, much more.

That is why my Department will be publishing an Energy Investment Report to supplement the work done by the Treasury and the Department of Business and Innovation.

It will capture investment across all energy sectors – from renewables to oil and gas, nuclear to energy efficiency – so the figures are there for all to see.

The Energy Investment Report will be published before the summer recess with regular updates, so that investment rates and projections are transparent.

But what is already clear is that the key elements of our reforms, aimed at securing the massive private investment required, are already having an effect.

By working with the grain of the markets, we are ensuring that Britain get the diverse energy mix it needs - home grown renewables, new nuclear, a switch from dirty coal to cleaner gas, and, when the technology is ready, carbon-capture and storage.

Our Energy Act 2013 is designed to build the world's first ever low carbon electricity market to work over decades to come.

And it passed its 3<sup>rd</sup> Reading in the Commons with the active support of all political parties with only eight votes against.

That political consensus is working now, to attract the long-term investment we need.

We must keep that consensus.

But let me turn to the second area our reforms.

The markets themselves.

## **THE STATE OF THE MARKET**

Energy prices and bills have been rising for much of the last decade.

The main drivers of energy price rises in recent years has been rising wholesale energy costs, and the need to upgrade energy infrastructure to ensure security of supply in the long term.

According to recent Office for National Statistics figures for household spending on electricity and gas bills, there has been an 8% per annum rise during this Parliament.

That's actually down from 12% per annum we saw under Labour in the last Parliament.

But this will be of little comfort to those who are struggling to make ends meet.

It is imperative that the markets, both wholesale and retail, meet the test of affordability for customers.

But it is important that we concentrate on what is actually causing the problem.

We can't control wholesale prices – but by encouraging home-grown energy – including renewables and nuclear – we can influence some of the costs over time.

But the best way to cut bills in the long-term is to cut our use of energy.

Some wanted us to turn our back on our social and environmental responsibilities by axing programs to help the fuel poor, improve energy efficiency and boost green energy.

But cutting energy bills by scrapping outright social and green levies would punish the fuel poor and punish future generations.

That is why the changes we made as part of the Government review of levies, which is reducing bills by an average of £50, protected the fuel poor.

Indeed we have extended by a further two years that part of the Energy Company Obligation that supports low income and vulnerable households.

And we have ensured that overall our new cheaper energy efficiency package will be carbon-neutral.

As a result, the major energy companies have confirmed, there will be no need for price rises in 2014, unless of course there is a major change in wholesale or network costs.

So how can we address the retail markets themselves to bear down on costs?

## **RETAIL MARKETS**

In 2010, the Coalition Government inherited a retail market with:

Too few competitors;

A confusing plethora of tariffs;

A distinct lack of transparency;

And a wholesale market also dominated by the Big 6 where they either supplied themselves or opted for over the counter deals, with no transparency.

For competition to work we need to make it as easy as possible for people to switch to suppliers who offer the best deals.

That requires transparency, choice and a convenient switching system.

So we have regulated to provide that.

Ofgem's tariff reforms have reduced the number of tariffs on offer from 350 in 2010 to fewer than 200 today.

New, clearer bill formats will be in place by March and all customers will be off dead tariffs by June.

And with the roll out of smart meters, so people can track their energy use, coupled with incentives for energy efficiency action through the Green Deal and other initiatives, we are putting consumers in the driving seat.

We are acting to simplify the switching system too.

It should not take five weeks for the change to take effect when you switch suppliers.

24-hour switching is my ambition, but I believe we can cut switching times in half by the end of this year.

In order for competition to work properly, people need a proper choice of who they switch to.

Between 2000 and 2010, the supply market contracted from 14 majors to just 6.

Now in 2014, because reforms put in place by this Government and Ofgem, Labour's Big 6 face 16 competitors.

The market share of the independent suppliers has gone up tenfold since 2010 to 5% - still not enough - but it is growing every day.

According to the latest statistics, compiled by Electralink and Energy UK, independent suppliers gained over 700,000 new customers in 2013.

And last month alone, just under 100,000 households switched to join independent suppliers.

With Ofgem's action to simplify bills and diversify the market, with industry action to reduce switching times, and with the growing popularity of collective switching schemes, I am confident we can maintain switching momentum in the long-term.

So we have acted to revolutionise the retail markets.

But we can do more, and must go further.

In October, I announced that Ofgem, working with the competition authorities, will report annually on the state of competition in the market, looking in depth and across the energy sector at profits and prices, barriers to entry and consumer engagement.

I have also asked Ofgem to deliver a full report on the transparency of the financial accounts of the energy companies and ways that that could be improved.

These reports will be published in the spring.

This week, I wrote to the Chief Executives of Ofgem and the Competition and Markets Authority to reiterate the importance of their independent analysis and the wide-range of possible recommendations available to them.

In addition, I suggested that they look closely at the gas supply market, which has been largely ignored by the current debate on energy bills, even though gas makes up the lion share of average annual energy bills for the vast majority of people.

These actions are forcing companies to open up their books.

And that means Government, the regulators, consumers groups and customers themselves are increasingly able to hold the energy companies to account for their pricing structures.

## **WHOLESALE MARKETS**

And just as the retail markets are being reformed, so are the wholesale markets.

Caroline Flint told IPPR just two months ago the share of energy traded in the day-ahead markets was just 6%.

Well that was the proportion when Labour left power.

But, in fact, day-ahead liquidity has been transformed.

Caroline appears not to have noticed, but during 2013 over half of all power was traded on these markets.

Ofgem will require the eight largest companies to report the volumes they trade through these markets to ensure these markets continue to strengthen.

So Labour's big idea to improve liquidity in the day-ahead markets through a pool is already out-of-date.

Reform to fix a problem I can understand, but to do so based on a misreading of the market is expensive, destabilising and purposeless.

The big barrier for independent generators is the forward markets.

And it is in the forward markets where there is now great scope to drive up competition and drive down prices.

Ofgem have now set in train an ambitious package of reform.

The proposed Market Maker reforms will provide independent generators and suppliers greater access to the power generated by the Big Six and other large power producers, enabling them to purchase and deliver cheaper energy to consumers.

And I am prepared to use the powers we put into the Energy Act to improve energy market liquidity should Ofgem's proposals be delayed or frustrated.

## **FALSE ANALYSIS**

So we have transformed the retail market, increasing competition, challenging the power of the Big 6 created under Labour, putting customers more firmly in the driving seat.

We have minimised the impact of Government policy on bills while protecting help to the poorest, protecting investment in low carbon and maintaining emissions reductions.

We are acting to bring far greater openness to the retail markets so the energy suppliers can be held to account for their prices.

And we are acting to increase liquidity in the wholesale markets, further boosting competition.

All these actions maintain the pressure that bears down on prices.

But these advances have been studiously ignored by the opposition.

And as a result Labour's initiatives are seriously flawed and would set back significantly the progress already made.

Not just the reforms to the market they are proposing, such as the pool.

But the proposal for an artificial intervention in the market to hold down prices too.

Put simply, Labour's blanket price freeze proposal is a punitive policy directed at the energy companies.

The rationale, as explained by Caroline Flint, is two-fold.

First, to address, and I quote, 'over-charging that has happened in the past.'

And second to create space to bring in market reforms that will address a market that is, and again I quote, "neither as competitive nor transparent as it should be".

The claim of overcharging is based on Labour figures claiming to show that, between 2010 and 2012, electricity prices had been deliberately inflated.

But, these figures have been comprehensively debunked by Cornwall Energy, which represents the growing body of independent suppliers, as demonstrating a complete misjudgement of how the markets operate.

Let me be clear, if the work that Ofgem and the competition authorities are doing shows that consumers are losing out as a result of market structure or practices then we will act.

But we should do so on the basis of proper evidence.

I have suggested Ofgem and competition authorities to look specifically at the domestic gas supply market on the basis of the summary of segmental statements Ofgem published at the end of November.

These statistics suggest profit margins are three times higher for gas supply than for electricity, with some companies making five times the profit and tending to charge the highest prices.

It is for Ofgem, OFT and the CMA now to consider - with regards to all the evidence - whether a market investigation reference is appropriate.

Labour have criticised me for drawing Ofgem's attention to these issues on the basis that the statistics are in the public domain, and there is nothing new to look at.

But, frankly, if that is the case, why did they not draw the same conclusion that I did?

Labour's approach seems to be to tar all suppliers with the same brush – the premise is they are all guilty of over-charging and should all be punished.

But blanket punitive sanctions against all energy suppliers on the basis of unsubstantiated assumptions is like condemning everyone who receives benefits as a criminal fraudster on the basis of Benefits Street.

Its political opportunism, pure and simple – and bad policy to boot.

What is interesting is that it's the small competitors challenging Labour's Big 6 who most oppose Labour's energy price freeze.

Why? Because a price freeze favours the Big 6.

If raw energy costs rise during a freeze, vertically integrated firms with deep pockets can withstand a profits squeeze that could bankrupt smaller retail-only firms.

As Ian McCraig, the Chief Executive of First Utility, the most successful new independents, said: *Bluntly, it could put me under...How am I going to absorb those costs? I only retail, I don't generate. The answer is, I can't.*"

Indeed, independent analysis, again by Cornwall Energy, suggest suppliers would have to increase their bills by up to £80 ahead of any freeze to hedge against wholesale price rises.

This would mean people paying higher bills over the period of any freeze.

So a price freeze is anti-competitive, reducing competition further rather than extending it, taking us back to square one again.

And it won't deliver the savings to consumers that Labour claim.

It also threatens to choke off the very investment in renewables and energy infrastructure that the country desperately needs.

Why invest in a country over the long-term when there is a risk of a Government that intervenes in such a ham-fisted way.

The 2013 Energy act provides stability and predictability, Labour's proposals undermine that.

And if Labour's price freeze is based on the premise of creating space for reforms that are obsolete and over-taken by events, as I have demonstrated today, that requirement falls.

They have wilfully ignored all the reforms the Coalition has made since 2010 in the retail and wholesale markets.

And, frankly, considering that Ed Miliband once had my job, we are entitled to expect a more statesman-like approach to energy policy than this.

## **CONCLUSION**

I began my talk today focussing on what unites us on energy policy rather than divides us and I want to return to that as I conclude.

In November 2009, in the run up to the last election, Ed Miliband gave a very thoughtful speech to the LSE, in honour of his father – the Ralph Miliband Lecture.

In this speech he talked of a new kind of politics – and a new way of thinking.

He argued that what he called the ‘politics of now’ – responding to short-term problems with short-term fixes – cannot tackle the hard choices that face us in energy and climate change policy.

He talked of ‘the politics of the common good’ – making choices based on the long-term needs of our country.

Building a new energy infrastructure to tackle climate change and protect energy security - protecting the poorest in the process – and ensuring that the costs of transition were as low as possible.

I couldn’t agree more.

I see what the Coalition has achieved in government as an extension of what he began as Energy and Climate Change Secretary.

The 2013 Energy Act, makes a reality of the 2008 Climate Change Act, and enjoys wide political support.

The market reforms we are enacting will embed fair play in the energy markets, putting consumers in the driving seat.

Together these help us along the path of meeting the energy trilemma.

Cutting emissions, protecting energy security, and delivering affordability for our citizens.

I don’t believe that everything is perfect, that is why we continue to act on behalf of the people of the country to hold the energy companies to account, increase choice and competition to bear down on costs, and work with our European partners to set the right framework for emissions reduction.

And in taking this work forward, I will do everything I can to maintain and argue for the political consensus that makes this possible.

Because that is what the politics of the common good demands.

**ENDS**