

# NERA

Economic Consulting

## **UK Energy Policy: Conflict between Security of Supply and Other Objectives?**

**Presentation at 24<sup>th</sup> Annual USAEE/IAEE Conference  
Capital Hilton hotel, Washington DC, 8 July 2004**

**Gordon MacKerron, Associate Director**



Marsh & McLennan Companies

# Main Issues

- What are they and why are they difficult to analyse well?
- How far do current risks to security require Government intervention?
- How far does pursuit of security conflict with other objectives?
- What is long-term relationship between security and environmental objectives?

# The new UK energy policy

- Radical cuts in carbon emissions
- Competitive energy markets/economic efficiency
- Security of supply
- Affordable energy

# Why worry about security?

Security always mattered, but between 1985-2000, markets seemed to take care of it – little new policy intervention. But c. 2000 (UK).....

- Oil market less stable, followed by war in Middle East
- Net natural gas imports imminent
- Gas becoming dominant primary fuel
- Various power blackouts, from California to Italy
- Doubts about whether new wholesale electricity market would produce enough generating investment

.....So security looked at afresh

# What questions should be asked?

- Is there a genuinely new risk to security? (problems of vested interests)
- Is there any serious barrier to markets managing the new risk? (risks and barriers often confused)
- Barriers may exist (eg market or Government failure: security has some 'public good' characteristics)
- If risks have risen and there are barriers, should Government always act to raise level of security? (Some levels of security may have been 'too high' in economic terms)

# UK security of supply issues

- Gas imports (But imports have advantages as well as drawbacks – issue is empirical, not one of principle)
- Network vulnerability (is investment adequate? Are licence conditions adhered to?)
- Will there be adequate generating investment in electricity (will markets anticipate Government intervention when wholesale prices high and thereby fail to invest enough?)

Overall, a limited case for new public policy intervention: beware special pleading from holders of high cost fuels/technologies

# Trade-offs: security and other objectives

- Governments still have to intervene if security problems are serious or acute enough
- Trade-off with economic efficiency: potentially serious problems in capital markets. Reduced incentives to invest to guarantee adequate security if markets believe Government will rescue either consumers or investors
- Trade-off with environmental objectives?
  - Will low carbon economy provide more or less security?
  - If renewables and conservation dominant, less demand for imported fuels, but possibly new risks of intermittency.
  - If nuclear and carbon capture dominant, other issues of generic nuclear faults/accidents
  - No determinate relationship



















