

21 September 2006

Dear Colleague

**National Grid's Winter 2006/07 Report September 2006**

Ofgem has published today National Grid's final Winter 2006/07 Document<sup>1</sup>. This signals the final phase of the consultation process to develop gas and electricity supply-demand outlooks for winter 2006/07.

This report reflects feedback on National Grid's May and July documents<sup>2</sup>. We very much welcome all of the views received from respondents and the time taken by everyone to feed into this year's enhanced consultation process. This feedback has helped National Grid develop its analysis of the outlook for the coming winter, and provide a more robust outlook for the industry and customers to plan for the challenges ahead.

At the time the initial (May) document was published, we identified a number of key issues and risks affecting the winter supply position. The July document provided an update on these issues. It is good to see that many of these risks and uncertainties have significantly reduced since July, in particular in relation to key infrastructure. But we cannot be complacent as new infrastructure may not be fully utilised and gas demand could be higher if significant problems were to arise with availability of non-gas-fired electricity generation<sup>3</sup> and if we have a very cold winter.

The Langeled pipeline, IUK expansion, BBL pipeline and Excelerate LNG project are all reported to be on or ahead of schedule. High levels of injection into Rough over the summer months also mean that the facility is on track to be full in October. We provide a brief update on each of these issues in this letter. However, the arrival of new infrastructure does not necessarily equate to the arrival of gas. Experience last winter tells us that the volumes that will flow into GB are still uncertain, meaning the potential for a tight winter remains, particularly if weather conditions turn out to be colder than average. We note that the Met Office forecast for the winter has also been published today.

On the demand side, National Grid has made a significant reduction in its gas demand forecasts since the May document because of the impact of much higher gas prices on demand for all customers, including domestic and small business customers. This has reduced National Grid's estimate of the levels of demand side response that could be required this winter (although we note that these figures are unchanged since the July document).

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<sup>1</sup> 'Winter 2006/07 Consultation Report, National Grid, September 2006,' available on Ofgem's website: [www.ofgem.gov.uk](http://www.ofgem.gov.uk).

<sup>2</sup> 'Winter 2006/07 Consultation Document', National Grid, July 2006; 'Winter 2006/07 Consultation Document', National Grid, May 2006, available on Ofgem's website: [www.ofgem.gov.uk](http://www.ofgem.gov.uk).

<sup>3</sup> We note BE's recent announcement about its Hunterston B and Hinkley Point B power stations. The announcement is factored into National Grid's report and analysis.

National Grid has not made any material adjustments to its electricity market assessment since the July consultation, other than a small upward revision to the headline plant margin to 22% (up 0.8%). With the gas supply/demand balance remaining tight, gas fired electricity generation is likely to continue to provide a valuable source of flexibility to the gas market as it did last year. Although the level of margin in electricity is healthy, significant problems in the gas market could spill over into the electricity market as some gas fired generation will be required during periods of peak electricity demand.

## **Key issues revisited**

Below we provide an update on the key issues that could affect gas supplies this winter:

### **Gas supplies**

- ♦ **the timely completion and utilisation of new import infrastructure:** The news on the new infrastructure front has all been positive. Langede has begun commissioning, IUK will be ready two months early – from 1<sup>st</sup> October, BBL reports that it continues to be on track for 1<sup>st</sup> December, and having gained planning permission for its Teesside import terminal, Exceleerate continues to be on track for an early January start and has announced that it has also secured LNG cargos for the UK;
- ♦ **availability of Rough storage facility:** At the start of the winter consultation process there was significant uncertainty about the availability of Rough following the incident in February this year. The Rough storage facility is now approximately 95 percent full and on track to be full for the start of winter, with full production rates expected to be available no later than 1<sup>st</sup> October. We also welcome the further announcement from Centrica Storage that an extra 55 mcm of capacity has been made available for this winter;
- ♦ **availability of UK North Sea gas supplies:** The South Morecambe field, which had been identified as the only other field using the same type of equipment that lead to the fire at the Rough platform, returned in August, ahead of the planned return date of September; and
- ♦ **availability of gas from Europe:** The experience of last winter demonstrated that the availability of physical capacity does not necessarily guarantee that gas will flow into GB, even when GB prices are at a premium to those on the continent. We welcome some positive developments on this front – for example the release of more storage data by companies such as GdF and Total. However, a number of uncertainties remain, and issues such as lack of information transparency still pose key risks this winter.

### **Gas demand**

As noted earlier, National Grid's estimate of the level of demand response required over winter has not changed since its July consultation. National Grid has however developed a number of new scenarios for this report – an initiative that we welcome. These scenarios are based on a set of historical weather patterns and serve to illustrate that in severe weather conditions, significant levels of demand side response could be required, particularly later in the winter. However, even under the most extreme scenario in the report (i.e. a 1 in 12 cold winter (using the Met Office base)), domestic gas supplies would not be threatened.

We are disappointed that gas DNOs have refused to provide information on the demand levels at which they would trigger their rights to interrupt customers. The table provided in this document is therefore based on the limited information received by National Grid in response to the May consultation, and represents a considerably less useful set of data than we had hoped would be available to help customers and suppliers form their expectations. This is an area of work that we would like to see developed as a priority over the coming months. National Grid and the other gas DNO's should give progress reports to operational and customer forums. In the event that the network companies fail to develop thinking in this area we will need to look to our regulatory powers to ensure that this information can be given to the market as expediently as possible and at the latest in time for the next winter outlook consultation.

### Consultation process

We would like to thank once again all those market participants, customers and other interested parties who have taken the time to attend any of our three Winter 2006/07 seminars to date. The seminars have been designed to give parties additional opportunities to participate in the Winter 2006/07 consultation process further than feedback received in the consultation. We have a final winter outlook seminar on 27<sup>th</sup> September in Birmingham, and will then be holding a series of 'Winter to Date' seminars at various dates and locations throughout the winter to continue to provide a platform for information sharing and debate on these topical issues:

Date	Title	Location
27 September 2006	Winter 06/07 Consultation Report	Birmingham
13 October 2006	Gas Contingency Arrangements	Manchester
10 November 2006	Options for Energy Buyers	London
20 December 2006	Winter to Date	London
24 January 2007	Winter to Date	Manchester
29 March 2007	Winter to Date	London
5 April 2007	Winter to Date	Glasgow

Could requests to attend any of these seminars please be sent to [wholesale.markets@ofgem.gov.uk](mailto:wholesale.markets@ofgem.gov.uk).

### Initiatives ahead of Winter 2006/07

Below, we set out an update on our own initiatives ahead of Winter 2006/07.

- ♦ **Working with government, customers and market participants:** We will continue to work to ensure that the government, customers and market participants are kept fully briefed on developments of the work undertaken ahead of and progress during next winter, for example via steering groups and our seminar series.
- ♦ **Demand Side Working Group:** We continue to chair the work of the DSWG, working alongside customers and shippers to identify and develop further ways in which potential barriers to providing demand side response can be removed.
- ♦ **Customer and Supplier seminars:** We have held a number of 'Options for Energy Buyers' seminars that are designed to help customers gain a better understanding of the commercial options which are available to them through a series of supplier presentations. We are continuing this seminar series over the winter, including a number of update seminars on the winter to date.

- ♦ **Information issues:** There will be greater information available to the wider market on gas flows onto the network this winter because of Ofgem's decision to approve UNC Modification Proposal 006 (effective 3<sup>rd</sup> October). We welcome the fact that National Grid has also taken steps to hold workshops relating to the release of this information to ensure the market is more ready/informed ahead of the winter. We note that a number of modifications have been raised relating to information flows, which we will be progressing once they have been through industry processes. We have also completed a number of meetings with major European suppliers and transporters and have shared what we have learned through our seminar series. We are continuing to push for more transparency in European gas markets and in GB where appropriate.
- ♦ **New incentives on National Grid Gas:** In response to feedback from customers, Ofgem has placed new incentives on National Grid Gas for this winter in relation to:
  - Improved website performance in respect of key market information; and
  - Improved gas demand forecasting.

These incentives were developed through discussions with the Ofgem led DSWG and Gas Safety Reserve work groups and will be in force from 3 October.

- ♦ **Gas safety reserve:** We are continuing our work to consider whether any improvements can be made to the existing safety monitor arrangements over the medium term.

### **Gas quality: technical study into blending opportunities**

National Grid published a summary of the study on the feasibility of blending at Bacton as Annex C in the July consultation update document. National Grid published the full report in August. The study indicated a good level of confidence in the physical mixing of gas at Bacton under the scenarios considered. But National Grid does not think it will be technically possible to make the necessary investment in new systems and measuring equipment to offer a blending service in time for this winter.

Given the potential importance of this issue, Ofgem hosted a gas quality workshop on 13th September. This workshop was well attended with presentations given by a range of GB and European TSO's, shippers and customers. There was overall agreement among attendees that, given the clear direction from government regarding the GB gas quality specifications out to 2020, gas quality is an issue that GB needs to address in the short–medium term. Following this workshop we are looking to establish industry work groups to assess the materiality of the impact of gas quality on gas flows to/from GB, and to consider the range of investment options (by potential locations and service providers) to address this.

We welcome the information provided to us by Fluxys on historical flows in Belgium. This information will enable us to develop different scenarios, which will help industry to establish the materiality of this issue and therefore feed into the investment appraisal process.

### **Beyond 2006/07**

New storage and import infrastructure which is due to come online over the next year or so may ease the supply situation for the next few years.

There is no room for complacency however, and we will continue to closely monitor the markets throughout and beyond the coming winter. In addition, we will face continuing challenges:

- We continue to push for further transparency and information from Europe. An electricity winter outlook report was produced on a Europe-wide basis last year by ETSO and will be published for the first time this year. Ofgem has pushed for an equivalent in gas, and GIE (the network companies' body) has agreed to consider the possibility of producing one for next year;
- The past summer has demonstrated that margin concerns can arise at any time of year, on both the gas and electricity markets. We are likely soon to be net importers of gas in the summer as well as the winter. Going forward, we will need to keep a close eye on the market over the summer months, and may need to consider whether a 'summer outlook document' is necessary;
- As described above, Ofgem is taking forward the issue of gas quality, in order to minimise any disruptive effect it could have on import flows in the coming years.

### **Way forward**

Finally, I would like to once again thank all those companies, customers and other key stakeholders who found the time to participate in National Grid's Winter 2006/07 consultation process - by either responding to the consultation documents or attending our Winter 2006/07 seminars in London, Edinburgh and Ferrybridge.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Alistair Buchanan'.

**ALISTAIR BUCHANAN**  
**CHIEF EXECUTIVE**