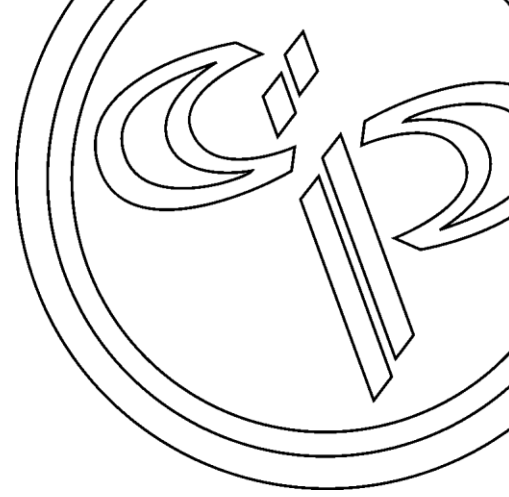


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CHARTERED INSTITUTE OF  
PURCHASING & SUPPLY®



Ian Marlee  
Partner, Trading Arrangements  
Ofgem  
9 Millbank  
London  
SW1P 3GE

Date: 20 November 2009  
Reference: Project Discovery - Energy market Scenarios

Dear Ian,

I am writing to you on behalf of the Chartered Institute of Purchasing & Supply (CIPS), the leading body for the purchasing and supply chain profession which represents the interests of over 50,000 buyers in 150 countries, 28,000 of which are located in the UK. Following the publication of the "Project Discovery" consultation, please find attached The Energy Committees' response to the questions posed.

Whilst we welcome the findings of project discovery we are also concerned that it has not gone into insufficient detail covering all possible scenarios. Our response contains questions around:-

- All the data has been averaged, which tends to smooth the peaks and troughs. Unfortunately the UK energy markets do not operate this way and it is the markets that send the investment signals.
- The Governments drive towards a low carbon economy leave many questions unanswered, namely:-
- De-carbonisation at any cost – what will be the impact of UK industry?
- National protectionism – With the UK leading the way, if all of Europe does not follow suite it will leave UK industry at a competitive disadvantage.
- The identification of the stress tests, whilst we understand that Ofgem must be thorough would it not be better to appoint a more general title to give customers more confidence?

We hope that our response and questions do not detracted from the very good work that Ofgem has carried out in producing this consultation. Please do not hesitate to get in touch if you have any questions regarding the points raised.

Kind regards

Martin C. Rawlings  
Chair CIPS Energy Committee

**Chapter 2. Approach and assumptions**

**Question 1:** Please provide comments on our approach of using scenarios and stress tests to explore future uncertainty, and as a basis for evaluating policy responses.

The approach is first rate, it allows for the evaluation of different factors and their impact on the United Kingdom.

**Question 2:** Are there other techniques for analysing uncertainty that we should consider?

Ofgem may wish to add a probability rating to each event?

**Question 3:** Do you agree with how we measure the impacts of our scenarios and stress tests?

We agree with how Ofgem have measured the impact of the scenarios and stress tests. However further investigation of the full impact we feel would be of benefit for example:-  
 1. the impact on GB PLC?  
 2. Business confidence?  
 3. Energy market volatility?  
 4. Impact as a hard cost?

**Question 4:** Do you agree with our key scenario drivers and choice of scenarios?

The Energy Committee agree with with Ofgems key scenarion drivers and choice of scenarios. Our only criticism would be that it is unlikely that global economies would all recover from recession at the same time. We believe that the event should be staggered for the impact analysis.

**Question 5:** Do you believe our scenarios sufficiently cover the range of uncertainty facing the market, and hence cover the areas where future policy responses may be required?

An under or over supply would have an impact, which your analysis does not take into consideration. Further, the scenario parameters may be a little wide i.e crude oil prices of \$200 to \$50 per barrel. What would be the impact if crude prices were \$130 per barrel?

**Question 6:** Do you have any specific comments on scenario assumptions, and their internal consistency?

Our only observation is that Ofgem's assumptions do not take into consideration the perponderance for nationalistic protectionism. Such behavior will have a dramatic impact on global supply. Further, can it be said that international markets always react to investment signals?

**Question 7:** Do you agree with our methodology for modelling gas and electricity supply/demand balances?

We are concerned that the modelling does not take into consideration gas daily flow rates and seasonality issues. Such omissions lead to missing stress points and skew the analysis results.

**Question 8:** Do you agree that LNG is the likely medium-long term source of "swing gas" for the European market?

Whilst CIPS agree that LNG is likely to be the medium to long term source we would also like to see seasonal storage and market price sensitivity taken into consideration.

**Chapter 3. Scenario analysis**

**Question 1:** Do you have any observations or comments on the scenario results?

The results do not appear to take into consideration daily market price volatility. A high level of market price volatility will almost certainly have an adverse effect on investment, as was experience in the late 90's. Further it would have a major impact on industrial and commercial customers that is not necessarily apparent by using annual average data.

**Question 2:** Do you agree with our assessment of what the key messages of the scenario analysis are?

Whilst we agree with Ofgem's assessment of the likely messages it is not clear as to the financial impact on GB PLC?

**Question 3:** Are there other issues relating to secure and sustainable energy supplies that our scenarios are not showing?

Your scenarious do not take into considerations GB planning & building regulations, whilst they have been relaxed to a certain extent, they will still slow down investment. Further the impact of other renewable energy sources such as wave power, bio-power, geothermal and solar power is not evident. Whilst these renewable sources of power are in their infancy, technology is such that they may become more cost efficient at a later date.

**Question 4:** To what extent do you believe that innovations on the demand side could increase the scope for voluntary demand side response in the future?

The rise in Automated Meter Reading equipment will make it easier for many I & C customers to participate in demand side response but only if they gain a financial advantage. Todate, the results from demand side bidding for interruptible gas has been far from a resounding success. Should the scenarios look at other incentives to encourage customers to participate?

#### Chapter 4. Stress tests

**Question 1:** Do you agree that our stress tests are representative of the types of risks facing the GB energy sector over the next decade?

CIPS consider that the stress test duration requires an indepth analysis to provide a more reflective outcome. In addition, whilst we would agree that Ofgem's stress tests are representative, we would like to see an expansion of volume/description to give greater transparency.

**Question 2:** Are there further stress tests that you think should be considered?

We would suggest that Ofgem look at the effects of multiple outages due common faults that customers experience every year i.e. The failure of stations in the nuclear fleet due to safety concerns due to aging plant. A further consideration is gas quality. For some time there has been concerns about the differential in gas quality between Europe and the UK. This subject has taken a back seat over the last couple of years but is beginning to become an issue again. Should Ofgem consider the implications of this issue?

**Question 3:** Do you agree with the assumptions behind our stress tests?

To understand the impact of interruptible contracts and enforced load shedding greater granularity in the information and data is required.

**Question 4:** Do you have any views on the probabilities of these stress tests occurring?

The global markets are such that there is always a probability that there will be an event. CIPS would suggest that the stress test titles be dropped for a more generalised title that will enable historic tracking to be facilitated.

**Question 5:** Do you agree with how we have modelled demand curtailment in response to constrained supply?

We are concerned that on how the demand side response figures have been derived as there is a volume amongst I&C customers that will not voluntarily curtail demand irrespective of financial reward. Has this been taken into consideration. Further, the volume used in I&C interruptible gas, has this been based upon current volume or post 2011 anticipated volume. This will have an impact on the outcome.

**Question 6:** Do you have any other comments on our stress tests?

CIPS would recommend that the stress tests not only look at demand but also at costs effects on I & C customers, which may have long term consequences. A further concern that CIPS has is the Government's drive towards a low carbon economy. De-carbonisation at all cost will have a dramatic impact on I & C customers. Our fears are that Europe will not follow the same course of action leaving UK industry at a competitive disadvantage. Ofgem's stress test should include such a scenario.