Annual Coal Industry Meeting 3rd February 2015

Agenda Items 2 - 7

Barnaby Pilgrim (Banks Group)

ITEM 2 – ENGAGEMENT WITH DECC DURING 2014

2014 Coal Forum Outcomes

"A Strategy for the Coal in the UK" – Discussion document from the Coal Forum Working Group

- DECC to formally respond to the presentation and comment on points raised
- Meetings to be arranged with cross-departmental officials to engage on specific issues including CPF
- DECC to consider input from Coal Forum in their engagement with wider industry groups and formulation of policy
- Maintain process of working and engagement with Coal Forum Working Group
- Coal Forum to report back to DECC on progress and issues

Progress

- Industry Engagement through 2014
  - Significant engagement between coal industry participants and DECC, HMT, DEFRA is acknowledged
  - Including companies, industry bodies and working groups
  - Input on key policy outcomes affecting coal, in particular CPF, Capacity Market, EPS and CCS
- 2015 - Next Steps
  - As will be discussed today 2015 is critical year for the future of full chain UK coal industry – mining, supply, infrastructure and generation
  - Coal Forum should provide forum for feedback, liaison, co-ordination between DECC and coal industry participants
  - Recommend quarterly meetings with Coal Forum Working Group and DECC/HMT/DEFRA
  - Establish clear agenda/actions/outputs
  - Quarterly feedback to DECC and Coal Forum members
  - Full Meeting of Coal Forum in Autumn 2015

John Campbell (Fergusson Group)

ITEM 3 – NERA STUDIES – CARBON PRICE FLOOR

NERA undertook rigorous and independent analysis of the potential impacts on the GB electricity market and broader UK economy of phasing out the CPS rate to harmonize UK and EU carbon costs

- "Improved affordability - lower wholesale electricity prices translate into reduced end user prices and savings for households and businesses."
- "GB supply security - the amount of coal capacity that chooses to invest in life extension more than doubles . . . enhancing UK energy security in the period before CCS is deployed at scale."
- "Economic growth - driven by greater household consumption and industrial output the UK economy grows more quickly."
- "Employment - higher economic activity prompts creation of additional jobs in the UK."
- "Government revenues - lost revenues from phasing out CPS are partially offset by higher tax revenues from increased economic activity . . . narrow based taxes such as CPS are more distortionary (have a greater deadweight loss) than broad based taxes."
- "Emissions - direct emissions rise, but impact is limited and converge to the same long term level . . . from an EU perspective the CPS is an inefficient and ineffective method of reducing greenhouse gases."

In summary, NERA analysis concludes that phasing out CPS after 2016 could deliver affordability, security and economic benefits via limited life extension for existing coal generation fleet - consistent with a managed transition towards UK emissions targets

- Recent wholesale energy price reductions do not alter key findings – coal generation is secure, economic and flexible, source of power providing long term hedge in volatile international commodity markets.
- First capacity auction outcomes consistent with NERA analysis – leaves only c. 6GW of coal plant planning life extension - out of 20GW capacity.
- 7GW coal capacity not awarded capacity contracts - concern that short to medium term commercial pressures and doubling of CPS may force plants to close earlier than predicted.
- Previous NERA work from Feb '14 indicated that CPS at £9.55 / tCO_2 could "provide an extended and more gradual phase-out of existing coal plants, enabling a bridge to CCS technology".
- As from April '15 the effective GB carbon tax is approximately 4.5 times higher than EU equivalent, placing UK at serious economic disadvantage on energy prices.
- **Recommendation – address CPS as a priority in 2015 Budget**

Luke Warren (CCSA)

ITEM 4 – CCS COMPETITION AND CONTRACTS FOR DIFFERENCE

CCS developments needed

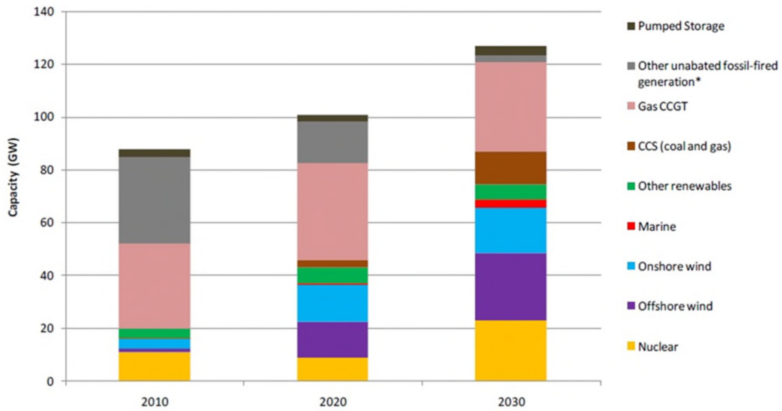
- Application of CCS to the coal-fired electricity plant now a reality
  - First plant began operating in 2014 (Canada) & another two under construction (USA)
- Firmly believe that UK is still well placed to be a leader on CCS
- Successfully conclude and deliver two projects from CCS competition
  - Retain £1 billion allocated for CCS at 2010 Spending Review and ensure access to CfDs under current LCF period.
  - Initiate two regional CCS clusters - key to delivering cost-competitive CCS and enabling wider deployment
- Early second phase projects needed if UK to have CCS at scale by 2030
  - CCS Development Forum agreed to advance CCS CfD
  - Key retain momentum on CCS CfD work in period to election
  - Enables new Government be in position to decide on phase 2

Philip Pearson (TUC)

ITEM 5 – CAPACITY MARKETS AND THE TRANSITION TO LOW CARBON

2030 capacity mix in fourth carbon budget advice

Figure 3. Capacity mix in a scenario underpinning the fourth carbon budget advice (2010, 2020, 2030).



Capacity market and low carbon transition

- DECC and CCC 2030 suggest c. 10GW of coal and gas CCS
- Accepted that future of coal in the UK is heavily dependent on the development of CCS from pilot to commercialisation
- But slower than expected roll-out of power and industrial CCS has many strategic implications: one threatens existing jobs in the coal supply chain
- A managed transition is needed to ensure a bridge from existing coal to new coal with CCS
- Outcome of the capacity market auction implies only 3.5 GW coal plant will invest to comply with IED (in addition to 2GW already committed) – less than one third of existing capacity
- This is insufficient to sustain the industry through to the CCS era
- Further change to the carbon tax regime would be required to bring forward necessary investment.
- Pace and scale of [I] CCS are crucial for power and industrial policy

Nigel Yaxley (CoalImp)

ITEM 6 – EMISSIONS PERFORMANCE STANDARDS

Risk of policies to phase out existing coal

- Last year saw renewed attempts by Labour to introduce an EPS on existing plant to prevent investment in pollution abatement equipment, following the first attempt in December 2013
- Forum members thank the Government for standing up for existing coal against these threats
- The risk remains that a new Government or Coalition will introduce an EPS or other draconian measure on existing coal – e.g. LibDem proposal for all plant to close by 2025
- Forum members do not expect existing plant to continue indefinitely but believe a gradual reduction by 2030 is preferable to a guillotine measure
- Government should stand firm on this issue recognising the value to the economy and to energy security/diversity of existing coal until replaced by coal with CCS

Phil Garner (Coalpro)

ITEM 7 – FUTURE OF UK MINING

Risks

- Market risks
  - Price is set by internationally traded coal and influenced by global supply/demand
  - UK customers are reluctant to enter into long term contracts
- Policy risks
  - CPS tax and its future trajectory or existence
  - Further attempts to impose an EPS on existing plant
  - BREF/BAT reviews of LCPD and IED? At EU level
  - Over-commitment from EU and/or UK as part of a global agreement
- Mining risks
  - Generally increase with depth
  - Reserve provenance to international standards requires significant exploratory expenditure
  - Supply chain support for mining products

Investor appetite

- In a global environment of a recovery from recession which is by no means without its own risks as it is still primarily driven by the economic growth of China and the other developing economies of South-East Asia, Investors are looking for low risk projects
- If all the risks identified on the two previous slides were acceptable there is still the message from politicians to the banking industry that they should not fund coal projects unless there is no obvious alternative source of energy
- NO WONDER WE ARE FACING THE CLOSURE OF DEEP MINES, LACK OF FUTURE SURFACE MINE PLANNING APPLICATIONS AND LOSS OF ACCESS TO MILLIONS OF TONNES OF COAL RESERVES IN THE UK!

Summary

- Coal Forum should facilitate liaison between DECC and industry participants in 2015
- Carbon price support should be reviewed in 2015 budget
- Retain £1 billion allocated for CCS and keep momentum on CCS CfD work in period to election
- Managed transition needed to ensure a bridge from existing coal to new coal with CCS
- Government should stand firm on EPS and policies to phase out existing coal generation
- UK mining faces multiple risks – positive messages from Government could help