RISING ENERGY PRICES – A SUMMARY

INTRODUCTION

Domestic electricity prices in NI are in the middle of the European range. However, NI energy consumers, like those across the UK and Europe, are currently experiencing sharp price rises.

This short note sets out the key reasons for rising energy prices and lists the actions that consumers can take to lessen the impact of further energy price rises in the future.

WHY ARE ENERGY COSTS RISING?

Reason 1: Rising wholesale costs on international markets

Household energy bills are mainly made up of the cost of networks and the wholesale cost of gas or electricity. The latter make up 60% or more of gas or electricity costs (see Figure 1). Network costs can be controlled in Northern Ireland through regulation, but the costs of wholesale gas or electricity are largely driven by Europe-wide or global trends.

Wholesale gas prices are currently at very high levels. Forward prices for winter 2008/9 on the British market (where all NI's gas is bought) are around 90% up compared to January 2007, while spot prices have risen even more sharply. These high prices are partly a result of high oil prices – gas producers often price in relation to oil prices. Also, importing more gas to GB in liquefied form is more expensive than traditional pipeline imports, while uncertainties about imports into GB, and a shortage of storage capacity, also drive up prices. NI has no gas storage at all.

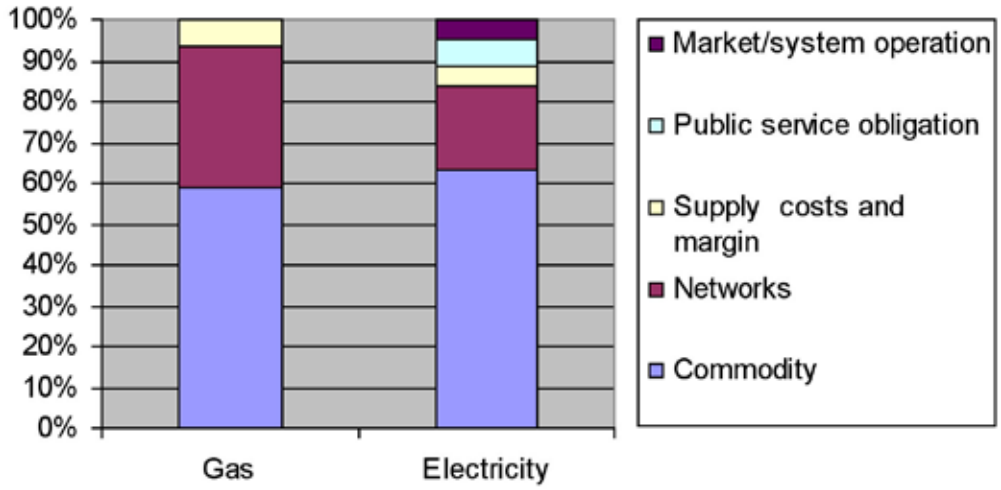

Figure 1- The make up of gas and electricity bills

Heating oil is also at record price levels, 60% higher since last year.

Reason 2: The costs of the key energy generation fuels are rising

Electricity prices are chiefly determined by the costs of generation fuels, which in Ireland mainly means gas and coal. As well as high gas prices, we are seeing coal at very high prices, over £70/tonne this winter, compared to a range of £28-£38/tonne during 1996-2006. These high prices are caused by high global demand for coal, and also shipping bottlenecks.

Reason 3: The cost of climate change

At EU, UK and NI levels, government accepts the need to prevent dangerous climate change. A fundamental part of this programme is to ensure that consumers pay all of the costs of energy consumption, including the cost of carbon. For this reason, the EU Emissions Trading Scheme (EUETS) caps carbon dioxide emissions and requires permits for emissions above this cap. These permits are tradable, which sets a market price for carbon.

This carbon price was very low in the first phase of the EUETS because high numbers of permits were issued, but has been higher in the second phase, since January 2008. From 2008, electricity tariffs here will reflect the cost of carbon for the first time (although the value of permits for electricity sold under NIE's long-term contracts is passed back to consumers, which will mitigate the effect in NI).

WHAT CAN NI DO TO REDUCE ENERGY COSTS?

Since November 2007, electricity has been traded in a single market across the island of Ireland, the SEM. In the short term there have been some small scale immediate costs, such as the costs of the new systems, which are already included in NI prices. In the longer term however, the SEM will bring substantial long-term benefits by creating more competition and incentives for new investment in efficient generators, both conventional and renewable.

The most certain way for NI consumers to reduce their energy bills is energy efficiency. This is a shared responsibility, with action from government, regulator and householders.

For instance, the Utility Regulator requires NIE to undertake a number of measures, and we have set up the Energy Efficiency Levy Scheme. This achieves significant, measurable energy savings each year. We have recently announced a review of the Levy Scheme, which will consider if the Scheme could be larger or more effective.

Utility Regulator
ELECTRICITY GAS WATER

Replacement of an oil boiler with a modern gas boiler and controls can boost effeciency by up to 40%.

Renewable electricity generation can reduce the impact of fossil fuel prices. The current government target is for 12% of NI's electricity to be renewable by 2010, but there is potential for much more.

However, this will require substantial investment in network reinforcement, new renewable capacity and also in conventional generation to back-up wind-farms. So growth in renewables can help NI consumers to avoid high and volatile oil, gas, coal and carbon prices, and mitigate price rises and price volatility, but it might nevertheless mean prices higher than current levels.

THE UTILITY REGULATOR'S ROLE

The Utility Regulator exists to protect consumers' short- and long-term interests.

We aim to secure value, choice and sustainable services for electricity, gas and water consumers by exercising our statutory powers. These include:

- Price controls to drive efficiency;
- Agreeing investment programmes to ensure sustainable development;
- Setting quality standards; and
- Promoting competition to improve value-for-money and choice.

We scrutinise proposed price increases by gas and electricity suppliers, and ensure these only reflect genuine costs.

In the last two years the Utility Regulator has achieved savings for consumers with a net present value of around £85m by driving price controls and mutualisation of network assets.

We will also continue to work with government, industry and consumer representatives on wider energy policy, to ensure NI is building a sustainable energy future.

For further information, visit www.niaur.gov.uk