

Written evidence submitted by the Investment Association

Energy Security and Net Zero Committee inquiry into our future energy technology mix

About the Investment Association

1. The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £10trn for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond.
2. The IA is proud to support the Net Zero Asset Managers initiative and to date investment managers responsible for three-quarters of assets under management in the UK have made this net zero commitment. Climate change is one of the single biggest systemic risks facing society and the planet today. The IA, representing the UK-based investment management industry, is committed to climate action and we produce an annual climate change plan, which outlines our commitments and actions we plan to take as an industry.¹ We support the Paris Agreement goal to limit global warming to well below 2°C, and preferably to 1.5°C, compared to pre-industrial levels, and the global goal on adaptation of enhancing adaptive capacity, strengthening resilience and reducing vulnerability to climate change. As investors, we see it as part of our fiduciary duty and in the interest of our clients, to help accelerate the shift to a net zero society.

Summary

3. The war in Ukraine placed great strain on European energy supply, coming at a time when an increasing number of households were already struggling with the growing cost of living. It is right that the Government should seek to address this while taking steps to mitigate the disruption to UK households. It is nonetheless essential that we have a long-term, predictable, and dependable plan in which the public and private sector can scale-up and make affordable and “everyday” the innovative new technologies and energy efficiency measures that will make the transition to net zero possible.
4. While we recognise that energy security may have become a more salient topic, it is also the case that energy security and climate change have been seen as concomitant concerns within UK policy for some time. While short term decisions may be deemed necessary to protect the security of energy supply today, it is also important to ensure that these twin priorities can coexist if a long-term strategy for either is to succeed.
5. The Climate Change Committee has commented that the Government’s Powering Up Britain strategy “included few new policies” and that the Government was still “lacking a credible overall strategy for delivering its objective of decarbonising the sector by 2035”. This assessment is echoed by the OECD, which commented that Government strategies “urgently need to be

¹ Investment Association, Climate Change Action Plan, July 2023, theia.org/climate-change-action-plan.

followed up by concrete and comprehensive policies in sectors where policy coverage is inconsistent with targets”.

6. We note that the Government consultation on the role of the Future System Operator (FSO) only recently closed, and that the Government intends to develop an action plan in response to the recommendations in the independent report of the Electricity Networks Commissioner. It is important that independent advice is now heeded and acted upon promptly, and desirable that the FSO should be granted a similar degree of independence.
7. The UK energy sector has undoubtedly shown itself to be open to new generation technology. Most notably, offshore wind generation is generally acknowledged to be a sector in which the UK is a world-leader. However, forecasts show that, among the world’s largest eight economies, the UK will have the slowest growth in low-carbon electricity generation between now and 2030.
8. With private sector investment so crucial to the UK’s clean and secure energy transition, it will be necessary to scrutinise the strategic plans (listed and private) companies have to manage this transition and to provide companies with an outlet to set out potential risks that could threaten an orderly transition. These plans will enable all stakeholders (including policymakers) to judge whether the energy sector is open enough to new generation technology.
9. Where companies remain closed to new technologies, the Government also retains the option of using a carbon price to incentivise investment by high-emitting sectors. The OECD has noted that the UK Emissions Trading Scheme has been “essential for the UK to nearly eliminate coal from electricity production”.
10. For the UK to attract investment there needs to be a solid pipeline of investible opportunities for investors to support. The IA supports proposals for a ‘UK Net Zero Investment Plan’ to catalyse the private finance needed. This must involve dialogue between private finance and Government departments to ensure investment supports orderly transition and sustains economic growth. The Net Zero Investment Plan would require Government departments to collectively assess the investment needed, track public and private financial flows across the economy towards the net zero objective, and provide a comprehensive and strategic financing plan to close the gaps between required and actual financial flows. In the absence of such a plan, it becomes even more important for departments and government bodies which are acting independently to take steps to analyse financial flows and actively leverage in private investment.
11. The Government should also continue to protect the achievements it has made in encouraging investment in the UK’s green transition. The UK green gilt is an achievement of the current Government which to date has raised in excess of £30bn for investment in projects including the Renewable Heat Incentive, the Heat Networks Transformation Programme, and the Social Housing Decarbonisation Fund. It is important to continue to build trust in the UK’s Green Financing Programme and provide investors with the confidence to continue to provide the long-term support so that the UK can adapt to climate risks and pursue green growth opportunities.

Is the energy sector open enough to new generation technology?

12. The UK energy sector has undoubtedly shown itself to be open to new generation technology. Most notably, offshore wind generation is generally acknowledged to be a sector in which the UK is a world-leader. The Government acknowledges that “offshore wind is essential to meet both climate change and energy security objectives” and has set an ambition to deliver up to 50 gigawatts from offshore wind by 2030 (including up to 5 gigawatts from floating wind, another new technology).²
13. However, Oxford Economics has forecast (for Energy UK) that the UK will have the slowest growth in low-carbon electricity generation between now and 2030 of the world’s largest eight economies.³ Senior executives at Ørsted⁴ and Vattenfall⁵ have both recently cited cost and uncertainty as factors that are likely to inhibit further investment in UK offshore wind. While the Government has stated it is “absolutely committed to maximising the vital production of UK oil and gas”⁶, a similar approach to maximising the potential for offshore wind may require a more active response to feedback from the offshore wind sector.
14. With private sector investment so crucial to the UK’s clean and secure energy transition, it will be necessary to scrutinise the strategic plans (listed and private) companies have to manage this transition and to provide companies with an outlet to set out potential risks that could threaten an orderly transition. The Government has shown welcome leadership in establishing the Transition Plan Taskforce, in which the IA participates, and with the FCA will consult on how to introduce transition plan requirements for UK companies. These plans will enable all stakeholders (including policymakers) to judge whether the energy sector is open enough to new generation technology.
15. Transition plans are, however, intended primarily to provide financially significant information relating to the net zero transition to investors including pension funds and their investment managers. Current, more limited reporting requirements have led BP⁷ and Shell⁸ to announce that they are scaling back plans to reduce oil and gas output and have provided an opportunity for investors and other stakeholders to question these strategies.
16. Where companies remain closed to new technologies, the Government also retains the option of using a carbon price to incentivise investment by high-emitting sectors. The OECD has noted that the UK Emissions Trading Scheme (UK ETS) – alongside the UK’s previous membership of the EU Emissions Trading Scheme (EU ETS) and the introduction of the Carbon Price Support – has been “essential for the UK to nearly eliminate coal from electricity production”. Since the UK ETS covers approximately 25% of current emissions, there is clear potential for the UK ETS to be expanded.⁹

² DESNZ, Energy Security Bill factsheet, July 2023, bit.ly/3YDxFSX.

³ Energy UK and Oxford Economics, The Clean Growth Gap, July 2023, bit.ly/3qzIQzE.

⁴ FT, ‘UK will struggle to lure new offshore wind projects, warns Ørsted’, August 2023, bit.ly/3slJuB6.

⁵ FT, ‘Blow to UK renewable plans after Vattenfall halts wind farm project’, July 2023, bit.ly/45y2pY3.

⁶ HM Government, Powering Up Britain: Energy Security Plan, March 2023, bit.ly/3slKsgl.

⁷ BBC, ‘BP scales back climate targets as profits hit record’, February 2023, bit.ly/3OVR7Hx.

⁸ Bloomberg, ‘Shell Challenged on Net Zero After Fossil-Fuel Investment Boost’, June 2023, bit.ly/3OXmUYq.

⁹ OECD, OECD Economic Surveys: United Kingdom 2022, August 2022, bit.ly/3QI1mAC.

Does the Government sufficiently support development of innovative energy infrastructure?

17. The Climate Change Committee (CCC) noted in March that while the UK Government has committed to decarbonise electricity supply by 2035, “the Government has not yet provided a coherent strategy to achieve its goal nor provided essential details on how it will encourage the necessary investment and infrastructure to be deployed over the next 12 years”.¹⁰ The Government has since published its Powering Up Britain strategy, but the CCC commented in June that this “included few new policies” and that the Government was still “lacking a credible overall strategy for delivering its objective of decarbonising the sector by 2035”.¹¹
18. This assessment is echoed by the OECD, which commented that the Government’s 2021 suite of strategy documents (including the Ten-Point Plan for a Green Industrial Revolution, the Net Zero Strategy, and the Net Zero Review “urgently need[ed] to be followed up by concrete and comprehensive policies in sectors where policy coverage is inconsistent with targets”.¹²
19. Nevertheless, the volume of work by the Government signals clear intent, which is boosted by recent individual announcements including Tata Group’s Somerset gigafactory and the establishment of two new CCUS clusters. We also note that the Government consultation on the role of the Future System Operator (FSO) only recently closed, and that the Government intends to develop an action plan in response to the recommendations in the independent report of the Electricity Networks Commissioner. Indeed, even the critical comments of the CCC (in its report Delivering a Reliable Decarbonised Power System) may be seen as part of a system which is pushing the UK towards a coherent and more detailed policy position. (In its 2022 Economic Survey of the UK, the OECD described the UK as “among world leaders in reducing domestic greenhouse gas emissions” partly due to a strong institutional framework which was “an inspiration to countries around the world”.¹³) It is important that this independent advice is now heeded and acted upon promptly, and desirable that the FSO should be granted a similar degree of independence.

Is the Government’s plan for energy security sufficiently long term?

20. The war in Ukraine and the economic isolation of Russia placed great strain on European energy supply, coming at a time when an increasing number of households were already struggling with the growing cost of living. The Russian invasion of Ukraine exposed vulnerabilities in the UK’s energy security, and it is right that the Government should seek to address this while taking steps to mitigate the disruption to UK households.
21. It is nonetheless essential that we have a long-term, predictable, and dependable plan in which the public and private sector can scale-up and make affordable and “everyday” the innovative new technologies and energy efficiency measures that will make the transition to net zero

¹⁰ CCC, Delivering a reliable decarbonised power system, March 2023, bit.ly/3YS8Sel.

¹¹ CCC, 2023 Progress Report to Parliament, June 2023, bit.ly/3OXgAiL.

¹² OECD, OECD Economic Surveys: United Kingdom 2022, August 2022.

¹³ OECD, OECD Economic Surveys: United Kingdom 2022, August 2022.

possible. This situation also highlights why it is essential that we plan for a future in which renewable sources of energy can help to provide power which is secure and sustainable.

22. While we recognise that energy security may have become a more salient topic, it is also the case that energy security and climate change have been seen as concomitant concerns within UK policy for some time. For example, in the 2009 UK Renewable Energy Strategy the Government described ensuring continued security of energy supply and tackling climate change as “increasingly urgent concerns”.¹⁴ While short term decisions may be deemed necessary to protect the security of energy supply today, it is also important to ensure that these twin priorities can coexist if a long-term strategy for either is to succeed. Public attitudes research by DESNZ which sought to understand public concerns about energy security in the summer of 2022 found the largest concern (at 87%) was that the UK is not investing quickly enough in alternative energy sources.¹⁵
23. Opinion research has also indicated public concern around the long-term viability of the UK Government’s net zero plans. Research between 2021 and 2022 by BritainsThinks (now known as Thinks Insight & Strategy) found that participants expected the Government to introduce and embed the measures needed across sectors of the economy to ensure that the necessary action was taken to reach net zero. Business, and then individuals, were regarded as having less responsibility. However, participants in BritainsThinks’ deliberative research project, The Net Zero Diaries, expressed a sense that the topic of climate change has been overly politicised, with policymakers overpromising to win support but underdelivering as they faced making tough decisions.¹⁶
24. The UK public continues to support the legal commitment to cutting carbon emissions to net zero by 2050. In July, a YouGov poll found that 71% of the public strongly or somewhat supported the net zero target, compared to a total of 16% who strongly or somewhat opposed it.¹⁷ In August, a poll by Opinium found that 51% of respondents thought the UK Government was underreacting to climate change, against 17% who thought the Government was overreacting. However, in the same survey 46% of respondents said they would strongly or somewhat oppose policies to combat climate change if they had a negative impact on their personal finances (compared with total support of 22%).¹⁸
25. Such results can help explain why a sense pervades that the UK Government’s plan for energy security is not sufficiently long term. We acknowledge the difficulty the Government may have in balancing overall public opinion on the energy transition and attitudes towards individual policies. In seeking a balance, policymakers may wish to look at the BritainThinks Net Zero Diaries where participants raised concerns in particular around how home insulation and heat pumps would be paid for but expressed particular concern on the potential burden on vulnerable and poorer households.

¹⁴ HM Government, The UK Renewable Energy Strategy, July 2009, bit.ly/44aJh0Q.

¹⁵ DESNZ, Public Attitudes Tracker, June 2022, bit.ly/444FeDu.

¹⁶ BritainThinks, The Net Zero Diaries, May 2022, bit.ly/3QG7QQU.

¹⁷ YouGov survey, July 2023, bit.ly/3qttpsP.

¹⁸ Opinium survey, August 2023, bit.ly/3sbE7EN.

26. Participants in the BritainThinks project – who were drawn from different backgrounds and viewpoints – were provided with information and access to expert testimony before forming their view. They concluded that there was a lack of connection and coherent strategy between different departments, a perception that government strategies to tackle climate change have been poorly monitored with performance against goals not met or tracked, and an absence of clear signposting for individuals or companies to play their part in the net zero transition. The group also suggested that a figurehead in Government showing strong leadership would “prove” that the net zero transition was a priority.

What energy generation mix will get us to net zero the quickest in the most affordable way?

27. Developing a new energy generation mix efficiently, and in a manner that is affordable for the Government and individuals, will require private investment. For the UK to attract investment there needs to be a solid pipeline of investible opportunities for investors to support. The IA has previously called for a ‘UK Net Zero Investment Plan’ to catalyse the private finance needed. This must involve dialogue between private finance and all Government departments to ensure investment supports orderly transition and sustains economic growth.
28. The Net Zero Investment Plan would require Government departments to collectively assess the investment needed, track public and private financial flows across the economy towards the net zero objective, and provide a comprehensive and strategic financing plan to close the gaps between required and actual financial flows. This investment plan should be subject to independent assurance. We also support the creation of a unit within government to produce and monitor the Net Zero Investment Plan and to ensure a whole-of-government commitment to delivery, in line with the model for an Office for Net Zero Delivery outlined in the Skidmore review. A wholistic plan, independently verified, would better enable assessment and attainment of value-for-money.
29. In the absence of either such a plan or delivery body, it becomes even more important for departments and government bodies which are acting independently to take steps to analyse financial flows and actively leverage in private investment. Such a priority is essential to ensure that all relevant bodies are equipped with the skills and resources necessary to engage with investors and the finance sector more broadly.
30. While there are disagreements on policy, the UK remains fortunate to experience a significant degree of political consensus – across parties and within devolved administrations – on the net zero transition and importance of energy security. This consensus should act as an incentive to invest in UK energy infrastructure. Nonetheless, political uncertainty remains a risk factor when parliamentary terms (and the potential for a change of government) typically operate on much shorter time frames than most major infrastructure projects.
31. While accepting that a degree of political uncertainty is a healthy and desirable feature of investing and operating in a parliamentary democracy, the Government might seek to capitalise on the widespread political consensus that exists in the UK to provide longer term certainty to investors. One means of achieving this would be to equip the FSO with a number of clear long-term mandates to drive policy delivery. These mandates should be agreed on a cross-party basis

and with parliamentary approval. These mandates must be sufficiently flexible to allow the FSO to be agile in delivery and properly consider the role of new and emerging technologies.

32. The Government should also continue to protect the achievements it has made in encouraging investment in the UK's green transition. The UK green gilt is an achievement of the current Government, for which the IA argued, and to date it has raised in excess of £30bn for investment in projects including the Renewable Heat Incentive, the Heat Networks Transformation Programme, and the Social Housing Decarbonisation Fund. According to the UK Debt Management Office (DMO) another £10bn in green gilt issuance is planned in financial year 2023-24.¹⁹
33. It is important to continue to build trust in the UK's Green Financing Programme and provide investors with the confidence to continue to provide the long-term support so that the UK can adapt to climate risks and pursue green growth opportunities. The Government must continue to champion the bond markets as a source of investment and consider how the DMO's developing expertise could be shared with other levels of government, particularly metro mayoralities.

Are the energy solutions universal across the UK or are there regional and local approaches on fuel and energy?

34. There may be areas that have historically had an abundance of natural resources (such as the oil industry in the north-east of Scotland), or otherwise deemed appropriate for a particular type of energy generation (such as coal-fired power stations). Similarly, there are areas which may now be well-placed to capitalise on the natural resources which are more in demand for the clean energy transition (such as wind and hydro). In choosing to plan for a future energy technology mix, it is essential that an overarching approach is taken that considers those who may consider previous opportunities to be in decline alongside those areas which stand to gain from the new mix.
35. In addition to local and regional approaches which focus on different energy types of energy generation, it will also be important for the clean energy transition to consider disparities in economic performance and skills across different parts of the UK. While the introduction of new technologies for the home provides an opportunity for every part of the country to develop a newly skilled workforce, the reality may be that without a systematic approach some areas may lack the resource to do so.
36. The OECD has stated that "there is a risk that unemployment increases throughout the transition if skills supply does not match demand." Housing energy efficiency and clean heating have been identified as particularly critical areas of need and it has been estimated that between 7,500 and 15,000 heat pump installers need to be trained each year until 2030.²⁰ The OECD recommends that "anticipating emerging skill needs and providing the up-skilling and re-skilling needed to limit labour market exclusion therefore should be an integrated part of policy measures to transit to net zero."²¹ This could be achieved by following the recommendation of the Electricity

¹⁹ UK Debt Management Office, UK Green Financing: Allocation Report, Sept 2022, bit.ly/3YA95CE.

²⁰ Green Jobs Taskforce, Report to Government, Industry and the Skills sector, July 2021, bit.ly/45xiUrw.

²¹ OECD, OECD Economic Surveys: United Kingdom 2022, August 2022.

Networks Commissioner that the Government should initiate an urgent review, involving industry and academia, to identify skills gaps and actions required to attract, recruit and retain the large workforce needed to deliver the net zero transition.²²

37. Investors may wish to see substantial commitments from corporate management to make their business practices more sustainable before they are willing to put additional capital at risk. Investors will consider companies' preparedness and resilience to severe economic shocks, the impact of our natural environment on economic opportunity, and how these risks can be effectively incorporated into the investment process. One important tool for investors to understand companies' preparedness for these trends will be in company reporting on approaches to management of staff through enhanced annual disclosures. Company disclosures should foster improved investor understanding of the role played by the company's workforce in generating sustainable, long-term value creation.
38. To achieve this companies should provide shareholders with a narrative within their Strategic Report (and where appropriate, in a Transition Plan) on the significant investments that the company has made over the past year, and is planning to make in the next, to improve the productivity of its workforce and the opportunities, and principal risks, relating to the company's approach to human capital management. The IA publishes long-term reporting guidance to assist companies' understanding of shareholders' expectations for Strategic Reports. It is increasingly important for companies to invest in the skills of their employee base to build resilience against longer term economic trends such as the greening of the economy.
39. It is also important that policy considers regional and local variations in how energy is used. There is much awareness at present of the impending ban on installing new oil boilers, but while the replacement of oil boilers with heat pumps may signal the beginning of a convergence in energy consumption norms for people living in remote areas and city suburbs, there is an equal possibility of divergence in habits for others. There are anecdotal reports of difficulties installing heat pumps in urban flats, for example. (Indeed, the chief executive of the Climate Change Committee recently told the Environmental Audit Committee that he was unable to replace his gas boiler because heat pumps are "a very difficult thing to put in" flats.)²³
40. While this is a problem that might partially be resolved with the training of a more skilled installation workforce, there is also an opportunity to consider whether other approaches, such as district heating networks, might be a viable solution. In Denmark around 65% of all homes are connected to a local heat network²⁴ and the UK Government-funded Place-based Climate Action Network (PCAN) argues "place-based opportunities and measures require local partnerships to optimise planning, coordination, and collaboration, on issues such as heat and energy efficiency".²⁵
41. Participants in BritainsThinks' Net Zero Diaries project demonstrated enthusiasm for community-based approaches, although most had no prior experience of them in their local area.²⁶ Where

²² Energy Systems Catapult, Electricity Networks Commissioner: companion report findings and recommendations, June 2023, bit.ly/47D0aVg.

²³ Environmental Audit Committee, Oral evidence: Mapping the path to net zero, July 2023, bit.ly/3KHqgwi.

²⁴ Embassy of Denmark, Written evidence submitted to the BEIS select committee, Nov 2020, bit.ly/3qxywYO.

²⁵ PCAN, Enabling Place-based Climate Action in the UK, June 2023, bit.ly/3sg4Ccl.

²⁶ BritainThinks, The Net Zero Diaries, May 2022.

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such an approach is originated and driven by local partnership, it is still important that projects are able to access sources of public and private funding. As argued above, DESNZ can play a role in tracking financial flows to such projects and taking steps to encourage investment if barriers are identified.

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