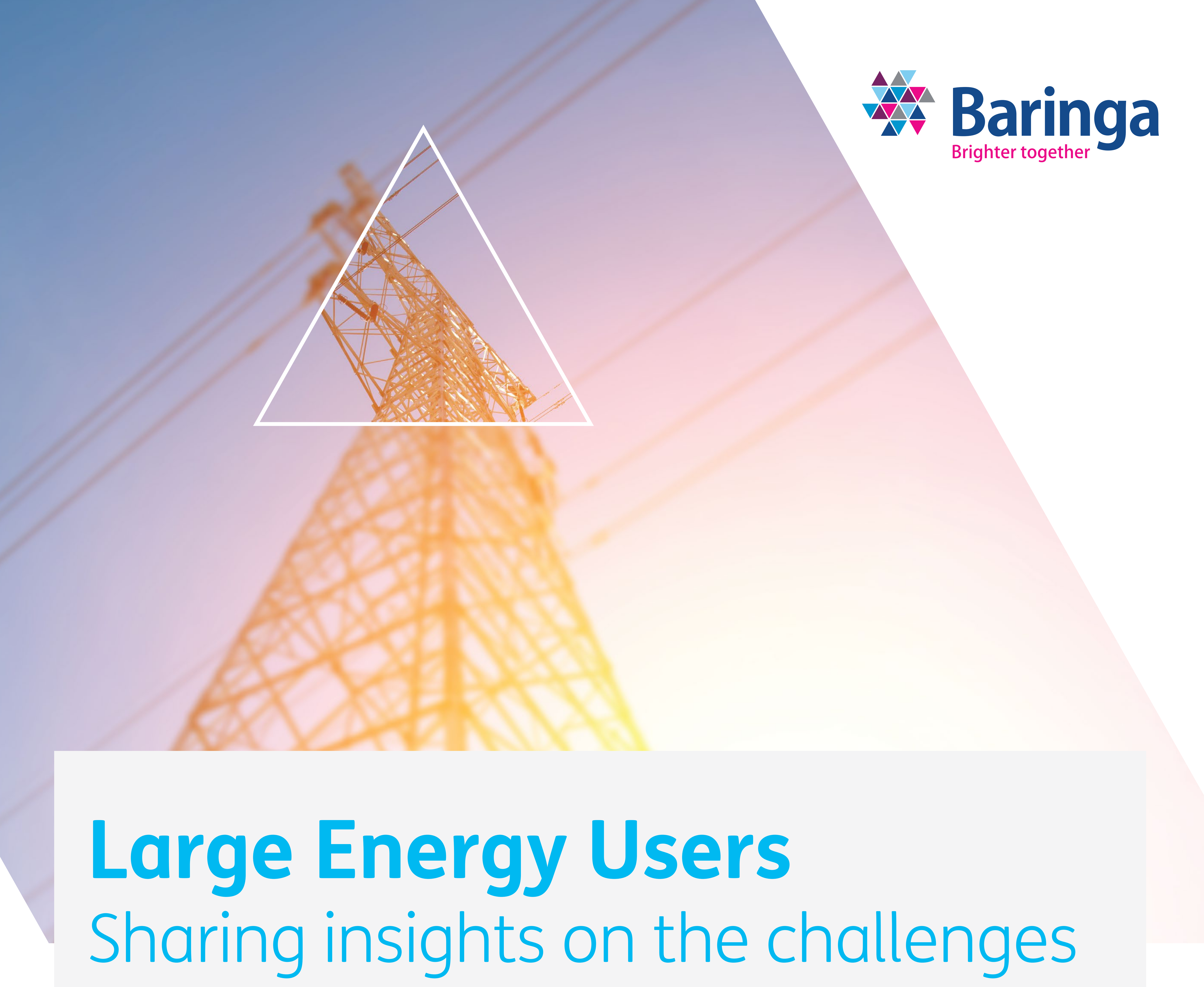

Baringa
Brighter together

Large Energy Users

Sharing insights on the challenges facing Large Energy Users

Baringa Partners hosted a breakfast roundtable discussion on 27th July 2017, attended by a group of thirteen multi-national Large Energy Users (LEUs) from a range of sectors, including energy infrastructure, fast moving consumer goods and media.

Baringa's Ilesh Patel, Jon Roberts, Stefan Gebski and Paul Stewart share their reflections on the discussion.

The Challenge: Rising costs, resilience, ambitious decarbonisation targets and asset management

A survey conducted at the event established that annual energy spend totalled over a massive £1.2Bn across the attendees. Energy consumption is a key driver of this spend, and most of the attendees expected this to rise in the coming year – with over half expecting the rise to be significant. Some LEUs felt that their organisation had a robust understanding of the current energy consumption as well as the forecast going forwards, supported by good data. Others, however, find this harder – particularly those organisations that are rapidly expanding.

Energy price is the other driver of spend. In particular, LEUs are particularly sensitive to rising non-commodity elements of their energy bill, such as network investment and renewable levies. These elements are mostly non-controllable, creating significant cost exposure for LEUs.

Unsurprisingly, the attendee survey highlighted that cost, therefore, remains the most important factor influencing procurement decisions.

Aside from absolute energy spend, LEUs face increasing challenges of ensuring resilience to their operations, particularly those that are considered mission critical. The theme of security of supply resonated both with LEUs in mature regions, where resilience can mean avoiding exposure to peak pricing, and LEUs in less established regions, where grid supply can be intermittent and black-outs common. Avoiding the impact of these events on core business has become an important theme.

In addition, LEUs are increasingly concerned with demonstrating a transition to decarbonised and sustainable business operations. As highlighted in the RE100 initiative, shareholders and customers of LEUs expect delivery of ambitious decarbonisation targets despite the rising pressure from cost exposures and operational resilience. Achieving these targets in the context of overall energy cost reductions has been a challenge for LEUs.

The Response: Energy Portfolio levers

1. More proactive engagement with Government, DNOs and renewable generators

Recent, rapid reductions in technology costs and the resulting changes to commercial drivers have created a disconnect between policymakers and energy markets. As policy makers scramble to address these shortcomings, LEUs face additional risks and costs as a consequence of reactive policy changes, both intended and unintended. There is an opportunity for LEUs to proactively and collaboratively engage in shaping policy directions that fairly address the long-term needs of all stakeholders.

In addition, engaging proactively with local Distribution Network Operators will also provide LEUs with an opportunity to secure better value for money when network utilisation and the need for flexibility increases.

There is a further disconnect between renewable energy generators and LEUs. While there is a mutual benefit to work together, historically objectives have perhaps been misaligned. Generators seek protection against falling marginal price/value, while LEUs are hesitant to sign a long-term offtake agreement in a rapidly evolving marketplace.

Overall, LEUs recognise the commonality in the challenges they face across industries and recognise the benefits of collaborating to engage effectively with industry stakeholders.

2. Clearer communications to senior executives of the underlying complexities and strategy

Within the LEU's organisation, there is often a misalignment to the overall corporate strategy. This has sometimes percolated to energy managers and executives, who find it difficult to articulate the complexities of the energy cost base and value chain across the organisation's operations. Additionally, there is a frequent misalignment between long-term funding priorities necessary for energy infrastructure and short-term payback expectations of LEU shareholders.

While the LEUs' requirements are increasingly sophisticated, they can choose their responses from a complex and growing range of available levers. A clear understanding and communication of asset data, cost exposures, risk appetite and a holistic/integrated strategy is critical to securing executive buy-in and funding, in addition to establishing the correct delivery model and selecting the right mix of solutions.

3. Find effective commercial and funding models that work for all

LEUs are increasingly looking towards a more sophisticated commercial model with their suppliers and other third parties where incentives and benefits can work for all involved. This applies both to conventional supply of energy via the grid and to more innovative energy solutions. Interestingly, our survey revealed a stark contrast in views regarding existing relationships with suppliers – approximately 45% said they were 'very likely' to change supplier, whilst another 45% said they were 'very unlikely' to change supplier. These polarised views indicate that many LEUs are actively seeking the right balance of benefits with a supplier, whereas many may already feel that they have struck a balance.

There is also a need for clear funding priorities. This is critical in a world where there is access to low cost of capital in the market against a drive from P&L owners to deliver shorter-term paybacks through operational cost savings. Energy buyers need to be able to build executive confidence and understanding to secure available longer-term value. In conclusion, finding an effective investment model, whether it be third party capital or converted to operational budgets, is an important lever.

For further information please contact Ilesh Patel on 0203 327 4220 or Ilesh.patel@baringa.com

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