

**Minutes of Expert Seminar on
'What are the key risks in the global gas and oil markets to 2030'
Monday 18 February 2008**

Chair: Paul McIntyre

Welcome and introductions (attendance list is at annex C).

The Chair welcomed everyone and informed that the discussion would take place under Chatham House rules and that a note of the discussion would be published on the BERR website.

Discussion

Tera Allas introduced the various scenarios as set out in Annex A. The following key points were noted during the discussion:

Identifying key scenarios and risks

- Other scenarios we needed to consider were:
 - Gas supplies locked up in bilateral deals in a non-global gas market resulting in constrained supplies and a constrained market;
 - The lack of liberalisation across the EU and its impact on competition and energy prices and flexibility of UK gas sourcing;
 - Risk of UK gas supplies becoming more concentrated and sourced from only a few supply routes, reducing flexibility and potentially introducing risks to security of supply
 - The threat of terrorism could increase the likelihood of supply disruptions, particularly when energy is being moved across great distances, hamper investment and increase the cost of oil and gas production;
 - Risk that UK gas infrastructure would not be built in time or would be insufficient.

Probability and impact on scenarios

The expert external participants' assessment of the probability and impact of the scenarios identified broadly in line with BERR's internal assessment, with an emphasis on the risks coming from deferred investment in both oil and gas and the lack of competition and liquidity in especially the gas markets (see Annex B). They emphasised the importance of understanding the implications of lack of European gas market liberalisation and competition and of Gazprom's strategy.

- There was an uncomfortable 10 years ahead as oil prices continued to rise. High energy prices could encourage people to use energy more efficiently but it would be incorrect to use this to influence policies. Government did not want prices to be higher than necessary to deliver its climate change goals.
- Proven oil reserves were concentrated in the Middle East and North Africa, together accounting for over 62 per cent of the world total. As a result, according to the International Energy Agency, OPEC's share of global oil production was projected to increase from around 40 per cent to around 50 per cent in 2030.
- Liquefied Natural Gas (LNG) could play a more important role in the future. However, because pipelines would remain the principal means of transporting gas, gas markets would remain regional in the short to medium-term.

- The expectation was that liberalisation would yield important short and long-term benefits in terms of improving economic efficiency, lowering costs and consumer prices and stimulating economic growth and competitiveness. The third EU package of EU measures would, if properly implemented by Member States, help provide the right regulatory framework to give the incentives for industry investment needed in gas. But energy markets in some Member States remained effectively closed. Chief among these were a lack of unbundling of some vertically integrated companies, a lack of transparency and ineffective regulation.
- Gazprom was opposed to European energy market liberalisation yet its influence in Europe was growing through bilateral supply contracts with some Member states and asset-swap type investments with European companies. Participants perceived there to be major risks attached to this as it could constrain supply and the market. The EU should speak with a single voice to ensure a coherent and unified approach.
- Participants expressed concern on managed gas markets in the absence of diverse supply routes and LNG terminals. Russia, the Middle East and Norway would continue to manage the markets by keeping much of its gas in the ground as the gas would be worth more in 10 to 30 years time. The squeeze on the supply side was not likely to go away soon.

Overview of UK current policy

International: The UK was committed to promoting open and competitive energy markets; take action to put a value on carbon emissions; drive investment to accelerate the deployment of low carbon technologies; and promote policies to improve energy efficiency.

Domestic: The government was driving forward its agenda on energy efficiency. The Energy White Paper sets out key messages around planning to encourage investment and to complete infrastructure on time. There was a political risk here which needed to be minimised.

Implications of risks for policy going forward

- While higher prices clearly have negative consequences for the economy, it should not be the Government's primary concern to lower fuel prices per se. Tackling global climate change would come at a price but we should not be concerned by this as the cost of failing to act far outweighed the economic costs of doing nothing.
- Participants noted that EU liberalisation had not been fully implemented but it remained a possibility. Furthermore, the prospects for further progress through the third package were not high. Did government have a Plan B if liberalisation failed?
- The UK should not opt to go down the bilateral route. Industry would not welcome government intervention at company level but it would welcome it at country level to ensure improvement to competition and to protect investment.
- A clear and stable regulatory regime was needed, including valuing for carbon, to reduce uncertainty for industry and to help ensure sufficient and timely investment. The planning system also needed to be improved and provide better information and analysis of long-term energy market trends to inform energy investment decisions.
- The one lever the HMG did have against monopolistic or oligopolistic rent seeking by oil and gas producers was tax: there was an implicit suggestion that this could be a useful issue to consider vis-a-vis gas markets where producers are currently making huge profits through oil-linked prices.
- Participants also agreed with the Government's policy to diversify the UK's energy sources wherever cost-efficient, and to create options for this in a low-carbon world (e.g., nuclear, CCS, renewables).
- The Foreign Secretary recently held a meeting on energy security with a number of other government departments at Ministerial level stressing the importance of it. The FCO had

also increased its resources in energy, both staff and money. But some thought that energy had fallen off the FCO's list of priorities when it last reprioritised its priorities. BERR would engage with the FCO on this.

Conclusions

The risks of tight fossil fuel markets and potential failure of liberalisation were clear. Not surprisingly, there was no silver bullet policy solution to avoiding or insuring against these risks. Rather, both the UK's international influencing and work with the EU, as well as domestic policies, needed to take these risks into account.

AOB

The Chair said that there would be a second seminar on renewables in Spring/Summer. However, the invitation list would not be exactly the same as experts would be invited according to the subject matter.

BERR
MARCH 2008

ANNEX A: AGENDA FOR THE EXPERT SEMINAR ON OIL AND GAS MARKET RISKS

Welcome and introductions

Session 1: identifying key scenarios and risks

Session 2: probability and impact of scenarios

Session 3: overview of UK current policy

Session 4: UK's international influencing agenda

Session 5: UK's domestic policies and actions

Wrap-up

ANNEX B: ASSESSING THE PROBABILITY AND IMPACT OF THE SCENARIOS

Scenario	Probability (H/M/L)	Impact (H/M/L)
A. Oil high NICs demand	Medium	Medium/Low
B. Oil deferred investment	Medium/High	Medium/High
C. Stronger OPEC	Low	Low
D. OPEC collapse	Low	Low
E. Peak oil	Low	Low
F. Gas high NICs demand	Low	Low
G. Gas deferred investment	Medium/Low	Medium/High
H. Gas cartel	Low	Low
I. Gazprom extends influence in Europe	High	High
J. No global gas market / gas supplies locked in bilateral deals	Medium	Medium/High
K. EU liberalisation stalls / competition not effective	Medium/High	Medium
L. UK gas import sources not diversified enough	Low	Low
M. UK gas infrastructure not built on time / sufficiently	Low	Low
N. Threat of terrorism on key infrastructure	Low	Low

ANNEX C: ATTENDEES

<u>Attendees</u>	<u>Company/Department</u>
Paul McIntyre (Chair)	BERR
Peter Hughes	BG
Brian Count	Progressive Energy
Peter Lambert	McKinsey
Barry Neville	Centrica
Darrel Sheinman	Energy Board
Geoff Horton	Horton 4 Consulting
Fergal Shortall	Bank of England
Richard Williams	Bank of England
Robert Woods	HMT
Martin Deutz	BERR
Tera Allas	BERR
Helen Dickinson	BERR
Ebba John	BERR
Andy Goodwin	BERR
Kanta Varsani	BERR (Secretariat)