

POLICY BRIEFING

RECONCILING ENERGY SECURITY WITH NET ZERO COMMITMENTS (UK)

June 2022

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To inform this briefing, the following investor group has been consulted: PRI Regional Policy Reference Group for the UK

THE PRINCIPLES FOR RESPONSIBLE INVESTMENT

The Principles for Responsible Investment (PRI) works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system. More information: www.unpri.org

ABOUT THIS BRIEFING

Responsible investment explicitly acknowledges the relevance to the investor of environmental, social and governance (ESG) factors in investment decision-making for the long-term health and stability of financial markets. As the Financial Stability Board has highlighted, the manifestation of climate change-induced physical risks, the risks of a disorderly transition, and the risk of a failure to transition to net zero are causing irreversible impacts on the socio-environment, and destabilising effects on the financial system. The risk of capital misallocation at a systemic level can threaten finance stability, with the International Energy Agency identifying \$26 trillion in capital re-allocation needed by 2040 to align with the Paris Agreement. A clear, consistent, and enabling policy environment is critical to the viability of the net-zero transition, and successful policy implementation helps minimise risks to the real economy, to individual entities and to the financial system as a whole.

The UK government published its [Energy Security Strategy](#) on 8th April 2022. This was developed to address energy security concerns and cost-of-living crisis, as escalated by Russia's invasion of Ukraine and subsequent economic sanctions. The latest [Queen's Speech](#), which was delivered on 10 May, also mentioned the forthcoming Energy Security Bill, which will detail plans to deliver on the *Energy Security Strategy* and enable a cleaner and more affordable UK energy system.

This briefing presents the PRI's analysis of the climate-related policies that would help leverage investors' interests in supporting the UK's journey to net zero and at the same time addressing concerns over energy security. If acted upon effectively, these measures would help fulfil the UK's commitments to 2030 and cement the UK's role as a global leader in climate action. The PRI develops policy analysis and recommendations based on signatory views and evidence-based policy research.

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THE COMPATIBILITY OF ENERGY SECURITY AND CLIMATE POLICY OBJECTIVES

The need to balance energy security concerns with short-to-long-term climate policy objectives is of great importance, particularly under the context of the ongoing global energy crisis. It is from this perspective that the UK has published its recent *Energy Security Strategy*. The headlines from the strategy are a five-fold increase in the target for offshore wind by 2030, a renewed spotlight on nuclear in UK's energy policy with the announcement of 8 new power plants and support for small modular reactors, green hydrogen. The Strategy states that 95% of British electricity could be low carbon by 2030.

Yet, safeguarding the robustness of these announcements and the UK's post-COP commitment on net zero are not without challenge. There is political pressure to relax restrictions on fossil fuel investments, including fracking, and allow the development of new oil and gas fields. There is also broader debate on how the energy security strategy will be financed and how net zero investments will be paid for.

As the UK Climate Change Committee (CCC) has commented, the ambition of many commitments listed in the Energy Security Strategy go beyond previous CCC proposals, particularly in deploying key low-carbon technologies, including offshore wind, nuclear, and hydrogen.¹ It also recognises that a reliable response to climate change is integral to the UK's future economic prosperity. Global leadership on net zero is also central to the COP26 presidency year for the UK.

Therefore, ensuring that the *Energy Security Strategy* does not conflict with net zero commitments is paramount. The following measures would be conducive to reconciling short-term energy security needs with the UK overarching climate objectives and continued commitment towards net zero:

- **Ensure that decisions made today, particularly short-term measures of using available energy resources to diversify energy supply, do not create lock-in of future emissions and new rounds of stranded assets.** Furthermore, these decisions should not derail the longer-term adjustments needed for infrastructure and the energy market.
- **Advance rapidly with existing plans outlined in the *UK Net Zero Strategy*,² including with consultations, sectoral policies, and enabling mechanisms to drive climate action and ramp-up private investment.**
- **Integrate the UK Energy Security Strategy with national development and policy planning,** to ensure that in the short- to medium-term, the UK government's Nationally Determined Contributions can be adequately financed and fulfilled. Specifically, the commitment is to reduce the UK's emissions by at least 68% by 2030 compared to 1990 levels.

¹ UK Climate Change Committee (2022) *Response to UK Government's Energy Security Strategy*: <https://www.theccc.org.uk/2022/04/07/ccc-responds-to-uk-governments-energy-security-strategy/>.

² UK BEIS (2021) *UK Net Zero Strategy: Build Back Greener*: <https://www.gov.uk/government/publications/net-zero-strategy>

POLICY PRIORITIES

The coming months will be crucial to ensure that the UK can increase its energy security while maintaining its mid- and long-term climate ambitions. The net zero transition offers countries and consumers a cushion against future supply-side shocks, which is of heightened importance to the UK, notably due to the cost-of-living crisis.

The following policy considerations are relevant to UK policymakers in preparation of the upcoming Energy Security Bill:

- **Pursue power sector decarbonisation at pace**, to support the UK and global net zero efforts and noting the benefits for energy security;
- **Prioritise actions to reduce energy demand**, such as **tackling building and heat sector demand**, boost energy efficiency, and accelerate policy progress in the *UK Heat and Buildings Strategy*³; and
- Deliver the *UK Net Zero Strategy* and Levelling-Up agenda in coordination to **enable a just transition** and ensure that the potential short-term costs for consumers are mitigated.

POWER SECTOR DECARBONISATION

A clean, affordable, and resilient power system is a key tenet of a net zero strategy and economy while electrifying other sectors. The International Energy Agency's (IEA) *Net Zero by 2050* report finds that all advanced economies, including the UK, should decarbonise their power sectors by 2035.⁴ As part of the UK's Nationally Determined Contributions (NDC), the UK government has pledged to cut greenhouse gas emissions by at least 68% by 2030, compared to 1990 levels.⁵ The UK's *Net Zero Strategy* also sets the target of fully decarbonising the UK power system by 2035.⁶

Several proposals balancing power sector decarbonisation and ensuring energy security were highlighted in the *Energy Security Strategy*, including the expansion of offshore wind, consultation on developing onshore wind partnerships, increased deployment of civil nuclear, and a new licensing round for North Sea oil and gas projects. The forthcoming Energy Security Bill should also contain elements towards increasing the integration of renewables in the grid.

However, it is important to recognise the declining role of fossil fuels in the global net zero transition, particularly considering the UK's decision to end financing, aid funding and trade promotion for fossil fuel energy sectors overseas.⁷ The **IPCC Sixth Assessment** highlight that, globally, continued fossil fuel expansion is not compatible with efforts to keep global warming to 1.5°C. A "rapid shift away" from unabated coal use and "cancellation of new coal power projects and accelerated retirement of existing coal plants" are needed.⁸ The **IEA's** *Net Zero by 2050* report also states that "beyond projects

³ UK Heat and Buildings Strategy (2021): <https://www.gov.uk/government/publications/heat-and-buildings-strategy>

⁴ International Energy Agency (IEA) (2021): *Net Zero by 2050* <https://www.iea.org/reports/net-zero-by-2050>

⁵ UNFCCC United Kingdom of Great Britain and Northern Ireland's Nationally Determined Contribution: <https://www4.unfccc.int/sites/ndcstaging/PublishedDocuments/United%20Kingdom%20of%20Great%20Britain%20and%20Northern%20Ireland%20First/UK%20Nationally%20Determined%20Contribution.pdf>

⁶ UK BEIS (2021) *UK Net Zero Strategy: Build Back Greener*: <https://www.gov.uk/government/publications/net-zero-strategy>

⁷ UK Prime Minister's Office (2020) *PM announces the UK will end support for fossil fuel sector overseas*: <https://www.gov.uk/government/news/pm-announces-the-uk-will-end-support-for-fossil-fuel-sector-overseas>

⁸ IPCC Sixth Assessment Report (2022) *Climate Change 2022: Mitigation of Climate Change*: <https://www.ipcc.ch/report/ar6/wg3/>

already committed as of 2021, there are no new oil and gas fields approved or development in [the IEA's net zero] pathway, and no coal mines or mine extensions are required."⁹ The **UNEP Production Gap Report 2021** finds that the world's governments currently plan to produce 57% more oil and 71% more gas in 2030 than would be consistent with the 1.5°C scenario and getting on track entails decreasing oil and gas production by 4% and 3% respectively each year until 2030.¹⁰ In addition to possible incoherence on climate policies, delayed and disorderly transition risks undermining the value of financial assets.

Domestically, while it remains imperative for the government to replace Russian oil and gas, the timescale of new UK oil and gas infrastructure would not reconcile short-term energy shortages nor be compatible with climate goals. According to data from the North Sea Transition Authority (then-Oil & Gas Authority), it takes on average 28 years for an oil and gas field to progress from first discovery to first production. Once fully approved, new fields take approximately three years to be constructed.¹¹ As the CCC has highlighted, additional domestic production will not significantly shift energy prices given the international market design.¹² Research by the Inevitable Policy Response, commissioned by PRI, also finds that strengthening national strategies and public finance for a credible just transition is critical in the current juncture. This includes phasing out fossil fuel subsidies and switching support to low-income households in the deployment of net-zero solutions.¹³ As such, bringing new fields online in the 2040s and 2050s would not provide relief for the energy security and cost-of-living crisis, but in fact heighten the risk of exposing the UK to risks of stranded assets, while being inconsistent with the UK's own climate plans and global net zero leadership role.

Amidst the renewed push for fossil fuel projects, the following should be considered:

- **Accelerate measures needed for the energy transition (many of which are the same as those needed to wane off reliance on Russian oil and gas)**, including clean investment step change towards retrofitting, grid infrastructure, increased flexibility, demand response, and long-term storage to build long-term energy system resilience;
- **Acknowledge that new fossil fuel infrastructure build in the UK goes against net zero objectives**, based on the IEA and IPCC scientific findings, the ineffectiveness of new UK fossil fuel infrastructure in reducing price pressures, and the incompatibility of the North Sea Transition Authority's licensing and consenting timeframe with UK climate goals;
- **Release phase-out plans for all UK support for coal, oil, and gas projects** in order to align with the UK carbon budget, interim and long-term climate goals.¹⁴

⁹ International Energy Agency (IEA) (2021): *Net Zero by 2050* <https://www.iea.org/reports/net-zero-by-2050>

¹⁰ UNEP *Production Gap Report 2021*: <https://www.unep.org/resources/report/production-gap-report-2021>

¹¹ UK Oil & Gas Authority *2018 UKCS Projects Insights Report*: <https://www.nstauthority.co.uk/media/6117/ukcs-projects-insights-report-2019.pdf>

¹² UK Climate Change Committee (2022) *Letter: Climate Compatibility of New Oil and Gas Fields* <https://www.theccc.org.uk/publication/letter-climate-compatibility-of-new-oil-and-gas-fields/>

¹³ PRI (2022) *The Just Transition: Shaping the delivery of the Inevitable Policy Response*: https://www.unpri.org/inevitable-policy-response/the-just-transition-shaping-the-delivery-of-the-inevitable-policy-response/9856.article#fn_link_8

¹⁴ PRI (2022) *The Just Transition: Shaping the delivery of the Inevitable Policy Response*: https://www.unpri.org/inevitable-policy-response/the-just-transition-shaping-the-delivery-of-the-inevitable-policy-response/9856.article-fn_link_8

ENERGY EFFICIENCY IN BUILDINGS AND HEATING

The CCC has outlined that to reach net zero, the UK's building stock needs to be nearly completely decarbonised by 2050, and the lack of adequate insulation measures can undermine the cost-effective deployment of low-carbon heat.¹⁵ Therefore, **improving energy efficiency is necessary for meeting the UK's carbon budgets and protecting consumers.**

The UK has the oldest building stock in Europe, and the least energy efficient housing in Western Europe.¹⁶ Building emissions have remained relatively flat since 2015, indicating a lack of policy progress in improving energy efficiency. Changes in supporting policies also stalled home efficiency improvement after 2012.¹⁷

As the government has detailed, 38% of the UK gas demand in 2022 was used for domestic heating.¹⁸ *The UK Heat and Building Strategy*, published in October 2021, sets out a policy direction towards a rapid scale-up of supply chains largely through market mechanisms, such as for heat pumps and heat networks, that require active policy interventions to remove barrier.¹⁹ **Further policy details for the medium-term are also needed.**

Currently, a gap in the *Energy Security Strategy* is new funding commitments to boost energy efficiency and help insulate buildings, particularly residential buildings. As research has indicated, the UK could **reduce its consumption of gas imports from Russia by 80% this year** through measures to improve energy efficiency and cut energy demand.²⁰ Therefore, the following enabling policy mechanisms would alleviate the cost-of-living crisis and ensuring energy security in the short-, medium-, and long-term:

- **Address policy gaps on energy demand, including on home energy efficiency**, and deliver funding to decarbonise public sector buildings and protect consumers amid the cost-of-living crisis;
- **Accelerate policy progress with planned consultations and policy papers as stated in the UK Heat and Buildings Strategy**, so as to ensure that proposals become concrete policies in the near-term. In particular, a major retrofit programme could generate jobs nationwide and stimulate local economies;
- **Continually monitor market development and ensure flexibility in intervention strategies** on both stimulating demand and supporting supply of heat pumps delivery and heat networks expansion, including direct policy intervention in case of a lagging market.

¹⁵ UK Climate Change Committee (2022) *Independent Assessment: The UK's Heat and Buildings Strategy*: <https://www.theccc.org.uk/publication/independent-assessment-the-uks-heat-and-buildings-strategy/>

¹⁶ UK Parliament (2021) Achieving net zero: energy efficiency of existing homes: <https://publications.parliament.uk/pa/cm5801/cmselect/cmenvaud/346/34605.htm>

¹⁷ UK Climate Change Committee (2022) *Independent Assessment: The UK's Heat and Buildings Strategy*: <https://www.theccc.org.uk/publication/independent-assessment-the-uks-heat-and-buildings-strategy/>

¹⁸ UK Government (2021) *UK gas supply explainer*: <https://www.gov.uk/government/news/uk-gas-supply-explainer#:~:text=Over%2022%20million%20households%20are,for%20industrial%20and%20commercial%20use.>

¹⁹ UK Heat and Buildings Strategy (2021): <https://www.gov.uk/government/publications/heat-and-buildings-strategy>

²⁰ E3G: *Dash from gas: the UK can quit Russian gas this year with rapid home energy saving drive* (2022): <https://www.e3g.org/news/dash-from-gas-the-uk-can-quit-russian-gas-this-year-with-rapid-home-energy-saving-drive/>

ENABLE A JUST TRANSITION TO SUSTAINABLE OUTCOMES

As the current COP President, the UK should continue to cement the commitment to 1.5°C internationally. Having strongly pushed to keep 1.5°C within reach in the Glasgow Climate Pact, and with the only national emissions reduction target consistent with 1.5°C as judged by Climate Action Tracker, the UK's climate policy focal point should rapidly shift to policy implementation and equitable delivery. This is especially the case for the UK as both a co-founder of the Powering Past Coal Alliance (PPCA) and a committed financier of Just Energy Transition Partnership with South Africa.²¹ This momentum should be captured to demonstrate pathways for the delivery and implementation for concrete, sustainable outcomes.

Drawing on the nexus between the Covid-19 pandemic and the climate crisis, it is apparent that the UK government has the social and economic capacity to devise emergency plans in a timely manner to protect vulnerable communities from the public health crisis. Similarly, for the climate crisis, delays in actions are not only costly but will exacerbate inequality in vulnerable communities. A successful *UK Net Zero Strategy* implementation should be achieved in coordination with the Levelling Up agenda, which includes investing in a nationwide green home retrofit scheme, coupled with long-term climate action to phase out of fossil fuels.²²

While the transitioning to meet the UK net zero goals is not without its challenges, it will also reduce costs for the economy, provide green jobs, put the UK on a sustainable growth path and provide opportunities for UK businesses and policymakers to share their expertise internationally.

The UK's commitment to being a world leader for global net zero is further substantiated by its greater responsibility and capacity to lead by action in the transition than many other countries, given the UK's access to renewable sources, technology, and its historical contributions. The following UK government policies would enable a just transition domestically and globally, and make finance flows consistent with a pathway towards net zero and climate-resilient development:

- **Establish a Just Transition Commission** to fully realise the UK's COP26 just transition commitments including facilitating stakeholder engagement, informing transition policymaking, forging consensus on phaseout plans in affected communities and providing financial assistance, education, or training that leverages resilient, green jobs for affected workers and communities;
- **Deliver the net zero agenda and levelling up proposals in coordination and strengthen harmonisation of UK climate strategies with devolved and local plans**, which warrants that UK regions' "Level Up" towards a greener economy is conducted in an equitable manner.

²¹ UK Joint Statement: International Just Energy Transition Partnership: <https://www.gov.uk/government/news/joint-statement-international-just-energy-transition-partnership>

²² Levelling Up the United Kingdom (2022): <https://www.gov.uk/government/publications/levelling-up-the-united-kingdom>

CLEAR POLICY ACTION INCREASES INVESTOR CONFIDENCE

While aspects of the *Energy Security Strategy*, if implemented rapidly as promised, could bring the UK closer to meeting its climate goals, it remains imperative to scrutinise policy gaps in the proposed strategy and implement enabling policy mechanisms that fulfil these gaps, as well as the Strategy's implication on the UK's wider net zero ambition.

Climate change poses significant risks for society and the economy, but the net zero transition also provides opportunities to build the industries of the future, support sustainable development and prosperity. **Investors are signalling their interests to invest in these opportunities, but to do so, they require reliable and concrete policies.**

The measures identified by the PRI would help establish clear near-, mid-, and long-term emissions reductions trajectories and plans and contribute to building the foundation of a resilient and secure economy that supports a rapid and orderly transition to net zero.

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More information: www.unpri.org



The PRI is an investor initiative in partnership with UNEP Finance Initiative and the UN Global Compact.

United Nations Environment Programme Finance Initiative (UNEP FI)

UNEP FI is a unique partnership between the United Nations Environment Programme (UNEP) and the global financial sector. UNEP FI works closely with over 200 financial institutions that are signatories to the UNEP FI Statement on Sustainable Development, and a range of partner organisations, to develop and promote linkages between sustainability and financial performance. Through peer-to-peer networks, research and training, UNEP FI carries out its mission to identify, promote, and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations.

More information: www.unepfi.org



United Nations Global Compact

The United Nations Global Compact is a call to companies everywhere to align their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption, and to take action in support of UN goals and issues embodied in the Sustainable Development Goals. The UN Global Compact is a leadership platform for the development, implementation and disclosure of responsible corporate practices. Launched in 2000, it is the largest corporate sustainability initiative in the world, with more than 8,800 companies and 4,000 non-business signatories based in over 160 countries, and more than 80 Local Networks.

More information: www.unglobalcompact.org

