

Funding the Future

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The UK has the highest domestic energy prices in Europe, and it's all down to poor regulation, political dogma, and the fact that we haven't got nationalised energy companies.

https://www.youtube.com/watch?v=ECTGhvVpsQc&si=Lw42IZWb_hMIAZ08

The audio version is:

https://www.podbean.com/player-v2/?i=bqvub-1794a2a-pb&from=pb6admin&share=1&download=1&rtl=0&fonts=Arial&skin=f6f6f6&font-color=&logo_link=episode_page&button-skin=c73a3a

The transcript is:

Energy prices are going up. And I do not think that they should be.

The energy price cap for the first three months in 2025 is going to be £1,738. Now that is the guide indicator issued by the energy regulator as to the amount that the average household with average energy consumption should be paying in the UK for its electricity and gas over the next three months, so it is not what your energy bill will be.

That cap has gone up. It doesn't need to. It's now roughly £600 more - even after prices have fallen dramatically since a year or so ago - than it was in 2021. In fact, from 2019 until early 2022, the energy price cap hovered at around £1,100 or £1,200 a year. Now, after the latest change, it's over £1,700 a year.

This is a massive cost for many British households. We know that there are many households that are in energy poverty. They're spending a significant part of their total disposable income on energy costs. And that's particularly true of pensioners, who obviously have a very low amount of money available to them for the purposes of living in any case. And we also know that Labour made that worse by taking away the winter fuel allowance.

So, I want to explain why energy should not be costing £1,738 a year in the UK. And why, in fact, it is that we have the highest energy prices in Europe, quite unnecessarily. And that's all because of the way in which energy prices are set in this country.

We have a quite absurd energy system in the UK. We have a system that was, of course, privatised under Margaret Thatcher and her successors in the Tory party. And they pretended, and we still do pretend, that there is a market in energy in this country.

We also presume that people are totally efficient. In other words, if you don't like your energy price from whoever might be supplying you today - call it Eon - then you know that British Gas will offer you a better deal, and you can afford to move costlessly from one to the other without any hassle and time involvement on your part and switch back again tomorrow if the balance of favour has switched back in Eon's favour. That's nonsense, of course, but that's what the energy regulator assumes because they think you're a rational economic human being.

They also think that we have energy production companies which behave in the way that market theory of economics suggests they should.

In other words, these are small companies, but no energy producer is a small company.

And they assume that they are subject to market competition. But the very point of having an energy regulator is because there is no market.

And they assume that they must be profitable at the point where their marginal costs equal their marginal revenues, which probably sounds like mumbo-jumbo to you, and is even in theoretical economics. But let me tell you what it means.

We make energy from a number of sources. Particularly, we make electricity from a number of sources in the UK. They used to include coal, but they don't anymore. They do include gas, solar, wind, hydroelectric, nuclear, and biomass, which is the Drax power station in the middle of the UK, which burns wood chips, imported at enormous cost to supposedly be a renewable energy supply, but which is anything but carbon neutral.

Those are our sources of energy supply, and the regulator assumes that the cost structure must make sure that every one of those is profitable, because, of course, they're not all owned by the same people. And if the energy regulator is going to

guarantee that all of those sources of energy are available to them, they must price energy so that every one of them is profitable.

Now, there's a dramatic problem with this. First of all, they use this marginal cost equals marginal revenue model, which is what economists would say is what defines profitability, even though I can promise you that is complete nonsense. But secondly, most of those sources of energy have no marginal cost.

There is no marginal cost to wind production.

There is no marginal cost to solar production.

There is actually almost no marginal cost to nuclear power production.

And that's because, in each of those cases, the vast majority of the cost of producing that energy is incurred up front, when you install the wind turbine, when you install the solar panel, when you install the nuclear reactor, or whatever. The actual cost of getting the energy after that is virtually nothing.

So, in those cases, there isn't a marginal cost to take into account with regard to determining what is profitable because there isn't such a calculation to be undertaken.

But there is in the case of gas. And there's a slight problem as a consequence because gas makes up, on average, around 40 per cent of UK energy supplies, although, on the morning that we're recording this, it's actually making up less than 10 per cent of UK energy supplies because it's pretty darn windy out there. But gas, because it has got a marginal cost, is the source of energy supply that is used to price all electricity.

But when you look at the total cost of production of electricity from gas and compare it with the total cost of production of electricity from solar, from wind, from nuclear - and they form the vast majority of the alternative sources of supply - what you discover is that gas is over three times more expensive than each of those.

So, the price of electricity might be set on the basis of gas, but gas is three times more expensive than every other form of energy, so we are therefore paying three times too much for our electricity.

Now, I'm not saying we're paying three times too much for our gas supplies. By and large, our supplies of gas are based upon the cost of supplying us with gas.

But when it comes to electricity, we are definitely overpaying. Because we assume that the gas producers of electricity have to be paid sufficient to keep them in the market, and everybody else must get the same price at the same time because that's what market efficiency supposedly requires, and, therefore, we overpay.

What's the consequence? Massive profit for some energy companies, particularly those

who are producing nuclear, and solar, and renewables. That is not good. Absurd.

If we had a nationalised energy industry, we would, of course, equalise the average cost of production with the sales price. How much would the price of electricity go down by as a result? It could be by up to a third. And of course, electricity is a major part of that energy price cap that we have to pay. So if we assume, roughly speaking, that half of that energy price cap is for gas and half is for electricity, then we could reduce that price by at least a sixth if only we actually treated the cost of electricity production as an average and not as a marginal cost to ensure that the gas producers are profitable. As a consequence, we'd all save maybe £300 a year, and wouldn't we all feel better off as a result, and Labour would have a fantastic time?

How would they compensate the gas producers? Because we do know we need them. Well, quite simple. We would actually not pay as much to the producers of nuclear power and turbine power and solar power as we do to the gas producers. We would equalize things out on an averaged basis, as would any nationalized industry that was in place to meet public need. We could therefore eliminate this excess profit from the whole supply chain of energy to us the consumer in the UK and considerably increase our well-being.

It would be quite straightforward, and the process of equalizing those costs within the industry could be done by formula without any difficulty at all.

So, why is it that our regulators carry on using a model that penalises us, the consumer, to benefit the producers enormously, because we know that they enjoy massive profitability?

And why is it that our politicians put up with that? Is it because they don't know that this is going on?

Is it because they hope that we don't know that this is going on and, therefore, won't notice that we're being bluntly screwed by the electricity price gap?

Or, is it that they are simply in blissful ignorance of the true nature of the economy and of the economics that is being used here and, therefore, are unaware of the fact that they're being taken for a ride, and so are we. I don't know the answer to that question. But it's about time they looked at this issue because it is wholly unnecessary for us to pay the price that we do for energy. It's time for a change.