

The Case for Energy Transition is Stronger Than Ever

As the world watches the troubling crisis unfold in Ukraine, the economic impacts of the conflict are becoming more clear. Several nations have levied strong sanctions against Russia impacting many sectors, and analysts say it could only be a matter of time before western allies impose sanctions on Russian energy exports, which could have major impact on the global economy. Recently, Brent Crude hit its highest price in nine years at \$118.22¹. Similarly, European natural gas prices also surged 50% to an all-time high of €185 a megawatt hour¹.

Heading into 2022, C-suite executives had expressed concerns about rising energy prices and rising inflation². Our recent FTI Resilience Barometer survey found that rising energy prices were the top concern of over 3,000 c-suite executives surveys from across the world. Linked to this, their second top concern was rising inflation. So, what is there to be done?

Energy transition

In Europe, for example, rising energy prices, spurred on by the Ukraine crisis, have stimulated conversations of national security and energy transition to help insulate countries from geo-political blackmail. Take for example how Russia supplies 40% of Europe's gas and at least 5m barrels a day of oil³; can any European countries really apply aggressive sanctions without fear of Russian retaliation through reduced energy supply?

If anything, the crisis in Ukraine has made many European countries realise the precarious position their reliance on Russian energy has on their economies. As a result, under the guise of national security, the Ukraine crisis has encouraged increased conversations about energy transition and in particular, local generation of renewable energy.

Essentially, the crisis has made national security (from a geo-political stand-point) and ESG unlikely but compatible bedfellows and is likely to accelerate Europe's energy transition. For example, Germany's decision to halt certification of the Nord Stream 2 gas pipeline.

Whilst obviously a geopolitical decision, this stance is likely to help Germany meet its ESG target to reduce carbon emissions by 65% by 2030 and perhaps even meet their target to reach carbon neutrality by 2045. Whilst it is not going to be easy, clear, lessons can be learned from Germany's approach.

1. Refinitiv (2022). Refinitiv Eikon [Online]. Available at: Subscription Service (Accessed: 02 March 2022)

2. FTI Resilience Barometer: <https://ftiresiliencebarometer.com/>

3. Bloomberg (2022) *Bloomberg Professional* [Online]. Available at: Subscription Service (Accessed: 02 March 2022)

This is something that is not only echoed at a national level but also at a corporate level: our recent global research highlights that 1 in 3 companies are facing increased pressure to improve on ESG and most companies are now shifting their approach to ESG from one of managing risk to one of seeing it as a business opportunity². How do companies (and or nations) do this?

Considerations for Energy Transition

Countries' (and indeed companies') abilities to implement effective Energy transition will depend on their starting points across three main levers:

1. Energy resource availability and technological readiness

- Current electricity generation mix and carbon intensity will play an important role in implementing a successful energy transition plan. Take for example Germany, which already has at least 40% of energy coming from renewables. In contrast, France has more than 65% of energy coming from nuclear power and South Africa has more than 80% coming from coal.
- In part these starting points are based on local availability of low carbon or renewable energy, such as wind, solar, geothermal, or hydro as well as technical/ technological capabilities present in that country.
- Lastly, technological readiness i.e., the condition of energy system infrastructure, is another important consideration. For example, does the electricity grid have sufficient capacity to add additional renewable capacity, and can it manage the variable supply loads that result from high penetration of some types of renewables?

2. Regulation environment and economic priorities

- A crucial hurdle in most Energy transition plans is the regulatory environments present in different countries; clearly, more accommodative fiscal policies would encourage more effective energy transition.

- There will however be a difference based on economic grouping, so for example, more developed economies can afford to push energy transition policies at a more ambitious rate and increase the penetration of low emissions technology before it is cost-comparable with existing technologies by offering subsidies or funding to consumers or private investors to switch to lower emissions technologies.
- This option is not available where country finances are more constrained and or economies that are burdened with higher levels of government debt and weaker credit ratings; after all providing energy at an affordable price to all citizens (among other basic needs) is a priority to these governments over energy transition.

3. Funding

- When it comes to the energy transition, perhaps one of the biggest sticking points is funding. Clearly, countries and corporates need to think more creatively about routes to market. These could include:
 - i. Increasing public-private partnerships;
 - ii. Using build-operate-transfer models for green infrastructure build (e.g., utility scale renewable energy power plants);
 - iii. Creating an attractive investment and operating environment for green industries (e.g., tax breaks);
 - iv. Taxing existing fossil fuel industries to create revenue for energy transition (e.g., a portion of EU ETS revenues go directly to EU climate and low-carbon industry funds)

Conclusion

Given the importance of energy on economic development, recent events have made it increasingly obvious that reliance on other sovereign states for energy places dependent countries in very precarious positions. Countries should now aim to transition their economies in a way that provides the most benefit for their citizens,

balancing short term needs (e.g., raising living standards and improving electricity access rates) with long term imperatives (minimising climate change impacts and building the skills and capabilities within their workforce/economy to benefit from new technologies).

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CLAIRE LAWRIE

Senior Managing Director –
Energy Transition

FTI Consulting

+44 796 6775 755

claire.lawrie@fticonsulting.com

LAURA MENZIES

Director –
Energy Transition

FTI Consulting

+44 781 2773 296

laura.menzies@fticonsulting.com

DR. NASH J MATINYARARE

Director –
Energy Transition

FTI Consulting

+44 792 9667 794

nash.matinyarare@fticonsulting.com

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