BCCG DISCUSSION PAPER

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OFFSHORE WIND UK - NEW BEIS REGIME TO HIT THE UK OFFSHORE WIND SECTOR

MAJOR RISKS FOR OFFSHORE DEVELOPERS AND INVESTORS... ...AND A PROPOSED SOLUTION

DR RAINER M. GIERSCH &
ROLF FYNE

BCCG ENERGY EXPERT GROUP

British Chamber of Commerce in Germany

A new BEIS regime is taking hold in the wake of Brexit.

As we forecast in our earlier discussion paper (The Green Revolution - UK's Ten Point Plan for Climate Neutrality by 2050; BCCG Discussion Paper March 2021) the UK Government is upping the ante for developers and investors in the UK's offshore wind energy sector on the North Sea continental shelf.
The Department of Business, Energy and Industrial Strategy (BEIS) are introducing much stricter regulations concerning the offshore wind developers' supply chain plans that are pivotal to developers' bids in auctions for Contracts for Difference (CfD). The new BEIS regime will tighten the already barely achievable UK content targets.
Formerly, Supply Chain Plans should achieve something around 50 per cent local content, meaning that half of the services and components needed for building offshore wind farms off the UK coast should be sourced within the UK. Time and again the 50 per cent could not be reached for a variety of reasons, mainly the non-availability of relevant major industry components, even with funding related training, research and university activities as a last resort.

The new BEIS regime creates incalculable risks for investors and government

Let's look at some examples:

There are no generators or turbines being manufactured in the UK, there are no monopiles manufactured in the UK, there is only a smattering of transition pieces and access platforms (TPs) being produced in the UK, tower fabricating having gone to the wall. No nacelles are being manufactured in the UK. These are an integral part of the turbines and consequently assembled where the turbines are produced. The list goes on and developers found a variety of excuses to duck out of their supply chain plan obligations or circumvent them. Half hearted attempts to placate BEIS were made by offering research funding to local east coast universities or dishing out service contracts to local providers. All true and good but with little real and lasting effect on the local economies.

Yes, there have been moves to establish solid UK manufacturing bases such as Siemens Gamesa with their wind turbine blade manufacturing plant in Hull and the adjacent marshalling yard for towers, rotor hubs, blades and turbines. Vestas also manufactures blades on the Isle of Wight supplying North Sea offshore wind projects. So real UK based contributions up and running which has eased access to UK supply chain plan content. But that depends on Siemens Gamesa or Vestas winning the contract to supply their turbines as other players come on the scene.

However, most of the time developers succeeded in finding a workaround if they did not comply with their proposed Supply Chain Plans. This also, because they were well aware that European law did not really allow the UK Government to introduce severe penalties if they did not.

Now we will see a situation where this will change.

The new rules set out by BEIS will not allow for any defaulting on agreed Supply Chain Plans. The SCP will become a firm part of the signed CfD.

At the same time, a massive expansion of UK offshore wind farms is in the pipeline

The UK Government in the 2019 Queen's Speech committed to delivering 40GW of wind energy by 2030, up from the 30GW agreed in the Offshore Sector Deal signed between Government and the Industry in March 2019. The Deal also calls for a more stringently policed 60 percent UK content by 2030 for the CfD qualifying developer Supply Chain Plan which may well increase as constraints disappear with the UK out of the EU Single Market.

In the Sector Deal, Government's BEIS also committed to biannual CfDs delivering up to 3GW annually. Looking ahead to the later 2020's, The Crown Estate's allocation of seabed for Round 4 opened up an initial 7GW to 8.5GW of seabed rights across four Bidding Areas, the two largest of 42,000 km2 in aggregate being in the UK North Sea Sector. Following a competitive tender in early February 2021, successful applicants included RWE Renewables securing two Dogger Bank sites each with the potential for 1,500MW and the GIG/Total consortium securing a site off the Lancashire coast also with a potential of 1,500MW.

The Government has also launched the Green Jobs Taskforce to help create two million green jobs by 2030 while the Offshore Industry has committed £250 million to support offshore energy skills and export development also by 2030.

The writing on the wall is there. The new ruling means that defaulting on Supply Chain Plan obligations developers have signed up to could result in severe penalties. The ultimate being the BEIS initiating termination of the CfD even as late as project completion.

Now, what does this mean for the developers and their investors?

Developers and investors will have to double check the feasibility and operability of their Supply Chain Plan right before bidding in a CfD auction to eliminate the risk of mid-way contract termination or worse by the UK Government that would result in the total loss of time and money invested.

The result will be that developers and their investors alike will either have to make sure that there is either substantial UK local content available or find a workaround that BEIS can sign up to that leaves no room for default. And it looks to us investors will have no choice other than work jointly hand in hand with developers from the outset in ensuring a feasible working supply chain plan. But can that be achieved with a dearth of UK content?

But there are also great risks for the Government

Should local UK content not be available and BEIS becomes unyielding, there is the probability that developers and investors will move their activities elsewhere - such as the up and coming US East Coast or to SE Asia. Japan being the next big offshore wind thing…

The new rules for UK content are a bit of a double edged sword.

The UK could be faced with a mounting lack of enthusiasm by international developers and investors in assisting in the UK's ambitious offshore wind program, thus forcing the UK Government to incentivise relevant elements of the offshore wind supply chain to establish on UK soil to guarantee the 60 per cent plus local content. This, in fact, probably is the only way to mitigate the developers' and investors' risk of contract termination down the line.

Investors and developers eyeing the UK offshore wind industry are well advised to give the current situation some more thought. We are aware that there is money to be made in the United Kingdom's offshore wind segment. 40 gigawatts should be generated by offshore wind turbines by 2030, which, given the current state of technology, means a total of around 2,300 new wind turbines to be installed. With the current 'strike price' of GBP 41.61/MWh and further new plants with around 29 GW capacity by 2030, this could result in a revenue potential of around EUR 4.9 billion annually, something not easily discarded.

Are there some timely solutions? In our opinion, there are.

A solution designed for European fabricators… but need to press the button now

The new situation strongly favours, for example, a UK East Coast Integrated Yard and Quay to manufacture offshore wind foundations, monopiles (MPs), transition pieces (TPs) and towers on the same site, a concept that has been worked on for some time and now, with the new tough Supply Chain rules demanding more UK content, time is of the essence.

To get the Integrated MP/TP/Tower Yard & Quay (IYQ) up and running two phases have been suggested.

This first phase brings potential IYQ partners around the table - MP/TP and tower fabricators, a UK heavy steel fabricator and investment partners - to take a first cut at the business case and the general shape of the IYQ site, quay and plant.

If it looks good, the partners would set up a Joint Planning/Production Engineering Desk with production/scheduling engineers/CAPEX/OPEX finance specialists from the partners working progressively evaluating site locations, shared fabrication and logistic resources across all components, production synergies and cost reductions and gaming scheduling options. Also engaging and working with UK sector Offshore Wind Farm (OWF) developers and investors, potential IYQ UK east coast sites and the BEIS.

The second phase would implement the Integrated Yard and Quay prefaced by registering the IYQ as an autonomous legal entity with shares held by the partners. An IYQ Project Team would deliver a complete physical working yard and quay to the IYQ management.

In parallel, the operations team recruit and train across all skills, work through 'set' sequencing and scheduling options and work with developers on buildout and ramp up timing delivering a fully functioning UK Offshore Integrated MP/TP/Tower Yard & Quay.

So what would be the outcome?

Accordo Partners, one of the proponents of this approach, estimates an East Coast Integrated XXL (Extra Large) MP/TP/Tower Yard & Quay would deliver upwards of 450,000 tonnes annually of lower cost MP/TP/tower 'sets' of UK content into Supply Chain Plans based on shared resource and production synergies. The avoided North Sea MP, TP and tower transport costs from continental Europe to the UK East coast operating port and associated insurance premiums will also contribute to driving down UK offshore wind sector developers' LCoE.

And a bite of the supply chain apple for real asset investors

A unique 'once in a lifetime' opportunity for real asset investors to finance this critical component of the UK's supply chain with the wind in the right direction driven by certain offshore developer demand and critical zero carbon political imperatives.

The first integrated foundation/tower yard and quay investment or any UK East coast 'market matching' monopile or tower capacity investment supplying UK supply chain CAPEX content, whether European or SE Asian, would lock out any further high capacity MP or tower investment in the UK.

It looks very much as if the European fabricators in the market are in a quandary. SE Asian corporates have already signed MOUs to set up a monopile manufacturing plant on the UK East Coast. A proposed investment which could take out approximately 300,000 tonnes of steel annually from European fabricators' North Sea markets significantly reducing European stakeholders' share of UK East coast business.

For the European players it may not be too late. Those European partners choosing to commit now to the proposed UK East coast IYQ as first movers might be able to secure the most vibrant, certain and derisked offshore market globally and simultaneously defend their North Sea and Baltic Sea markets.

But they need to decide now….

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Authors:

Dr Rainer M. Giersch, Chairman Hamburg/Northern Germany, Accordo Partners Ltd
Rolf Fyne, Founding Partner, Accordo Partners Ltd

Contact:

Ilka Hartmann, Managing Director & Member of the Board

Friedrichstr. 140
10117 Berlin
Germany

Tel.: +49 (0)30 206 70 80
Fax: +49 (0)30 206 70 829
E-Mail: info@bccg.de
www.bccg.de