



PRIME MINISTER'S QUESTIONS: 21 MAY

MONOPOLIES AND MERGERS COMMISSION REPORT ON THE CEGB

BRIEF

In her statement yesterday on publication of the MMC report on the CEGB, Mrs Oppenheim said that the Commission had "seriously criticised certain aspects of the Board's operations where there is significant scope for reductions in cost and for improved efficiencyAs levels of costs and efficiency are reflected in the prices paid by domestic and industrial consumers for electricity, it is important that improvements should be sought". Mr Glyn England, Chairman of the CEGB, is reported in today's press to have reacted sharply to this comment, saying "It was what she wanted the report to say, but it does not." ("The Times" 21 May 1981).

2. There is justification in the report for what Mrs Oppenheim said. The Commission found there were several respects in which costs had been higher than they might have been: ^{mainly} ~~outstandingly~~ because of ^{and past forecasting of future capacity and additionally} deficiencies in power station investment appraisal because of the Board's coal purchasing policies, and because of the Board's 'buy British' policy in the procurement of plant. There were in addition several comparatively minor matters where the Commission pointed to scope for improvement.

3. It is also true that the Commission commended the Board's behaviour in some respects, particularly in its day-to-day operational management. Mrs Oppenheim's statement acknowledged this.



LINE TO TAKE

I am satisfied that my rt hon friend's comments were fairly based on the content of the Commission's report.

Department of Trade

21 May 1981

Prime Minister,

FUTURE ECONOMIES

CEGB,

34
- Power
Station
Construction.

For the future the Board will need to pay particular attention to power station construction and fuel costs. Together these constitute the major element of its costs. I cannot emphasise sufficiently that power stations must from now on be built to time and cost.

This message comes through very clearly from the MMC Report. It is of fundamental importance to future electricity costs and thereby to British industry.

Generating Costs

Provisional CEGB figures for the annual cost of generation in 1980/81 in power stations commissioned between 1965 and 1977 are in pence per kilowatt hour

Hinkley Point	AGR	1.4
Magnox		1.7
Coal		1.9

These are historic cost figures and do not provide a basis for future investment decisions.

21 May 1981

MAP

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MMC REPORT ON THE CEGB

NUCLEAR POWER

Q WILL THE GOVERNMENT ABANDON THE NUCLEAR PROGRAMME IN THE LIGHT OF SCATHING MMC CRITICISM OF THE CEGB'S FIGURES?

A Nuclear power's contribution to our energy supplies is necessary in an uncertain world. We have always made it clear that each power station order will be considered on its own merits including its economic merits at the relevant time.

Q WHAT ACTION IS THE GOVERNMENT TAKING TO IMPROVE THE CEGB'S INVESTMENT APPRAISAL?

A The Secretary of State for Energy has already asked the Board for urgent proposals for improvements. The Board has itself acknowledged the criticism and said that it is seeking outside advice on possible improvements.

Q WILL THE GOVERNMENT NOW TELL THE CEGB TO BUILD COAL FIRED POWER STATIONS?

A The Board already has plenty of coal-fired capacity. Their provisional accounting figures for 1980-81 show that the generating cost for nuclear electricity was cheaper than that for coal-fired electricity - though they stress that these historic figures are not a guide to future investment.

Q WILL THE GOVERNMENT NOW RECONSIDER THE HEYSHAM AND TORNESS AGRS?

A No. The Government considered industrial and energy policy factors as well as the economic aspects, when the decision was taken to allow the Generating Boards to proceed with these stations.

Q HAS THE CEGB MISLED THE GOVERNMENT OVER NUCLEAR POWER?

A The Government knows that there must be major uncertainties in assessing a long-lived investment like a power station. But the Secretary of State for Energy has already asked the Board for urgent proposals for improving their investment appraisal in the light of the MMC report.

PRICES

Q THE MMC SAY THE FINANCIAL TARGET IMPOSED BY GOVERNMENT WILL RAISE ELECTRICITY PRICES. WILL THE GOVERNMENT RELAX THE TARGET?

A The Government keeps the target under review in the light of changing circumstances, including the fall in electricity demand since the target was set in January 1980.

COAL

Q WILL THE GOVERNMENT BACK THE CEGB IN AN EFFORT TO IMPROVE ON THE TERMS OF ITS UNDERSTANDING WITH THE NCB?

A The understanding is a commercial matter for the two Boards.

Q WILL THE GOVERNMENT RECONSIDER ITS ACQUIESCENCE IN THE POLICY OF BRINGING COAL IMPORTS DOWN TO AN IRREDUCIBLE MINIMUM?

A NCB coal is and has been competitive with imported coal at all but certain coastal sites. The Government recognise that imports can be a valuable yardstick for NCB's competitiveness. That is why there has been no challenge to the CEGB's right to import, and arrangements to reduce imports have been worked out in a competitive framework. In the tripartite discussion, the Government have agreed to help the NCB and the CEGB with the costs of displacing imports: arrangements for doing so are now being discussed.

BACKGROUND

NUCLEAR POWER

The MMC find that in respect of their investment appraisal, with particular reference to nuclear power, the CEGB are pursuing a course of conduct against the public interest. The Commission accept that it is right to appraise power station investment on the basis of a discounted cash flow calculation of lifetime costs and benefits, taking into account the effects of the station on the operation of the system as a whole. However, they severely criticise the assumptions and judgements used by the CEGB in their assessment, and conclude that a major new programme of nuclear power investment is proposed on the basis of inadequate investment appraisal.

The Secretary of State for Energy has already asked the Board for urgent proposals for improvement in their investment appraisal. The Board themselves have said that they are seeking outside advice on possible improvements.

However, it is not the case that a whole programme of nuclear stations rests on current investment appraisal practice. The statement by the Secretary of State for Energy in December 1979 made it clear that the level of ordering of nuclear power stations would depend on the development of electricity demand and the performance of industry. Each project will be appraised on its own merits.

Provisional CEGB figures for the actual cost of generation in 1980-81 in power stations commissioned between 1965 and 1977 show lower costs for nuclear generation:

	p/kWh
Hinkley Point AGR	1.4
Magnox	1.7
Coal	1.9
Oil	2.6

These are historical figures, and do not provide a basis for future investment decisions.

COAL

The answers to questions summarize the position in the tripartite talks with regard to imports.

The NCB/CEGB understanding is a matter for the two Boards - but it is intended as a ceiling rather than a floor on coal price increases.

ELECTRICITY PRICES

The MMC report points out that coal has always been the CEGB's principal fuel, and concludes that, even if their recommendations were fully implemented, they offer no early prospect of comfort to the CEGB's customers by way of real price reductions, especially while all fuels are becoming dearer.

The Secretary of State for Energy will be inviting the Electricity Council to take the MMC's views into account in the review of the CEGB Bulk Supply Tariff (BST) which the Council is already undertaking at his request.

Electricity prices are set to reflect the cost of replacing capacity needed to meet continuing demand. The move to Current Cost Accounting (CCA) by the electricity supply industry is in accordance with general accounting standards and bring accounting costs more closely into line with the true costs of electricity supply on a continuing basis. The move to CCA was taken into account in setting the industry's financial target, and has not in itself led to any increase in electricity prices.

ECONOMIES BY CEGB

The MMC commended a number of aspects of the Board's operations - for instance, revenue cost control, cash management, and internal audit - and their report paid tribute to the dedication of the Board's staff.

In 1980-81 the CEGB achieved:

- a) the lowest power station oil burn since 1963-64; oil purchases were sharply reduced, and flexible operation of oil-fired stations saved £5m.
- b) winter availability of single shaft 500MW/660 MW units of 87.8% - substantially up on 1979-80.
- c) highest ever thermal efficiency of fossil fired plant - 32.17% - to which the Board attribute a saving of £25m.
- d) saving of £2m through a shift in the balance between security of supply and cost of production.

Six power stations were decommissioned in 1980/81; 22 more will follow this year.

A net reduction of staff of 2340 was achieved during the year, with a substantial number of these coming from Headquarters formations. This saves over £20m a year after taking into account redundancy and severance payments.

Maintenance costs were reduced by £60m over initial plans.