Plot Your Path to Net Zero

A Focus on Funding

#RoadToNetZero

npower Business Solutions

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Introduction

The UK is now on a 30-year journey to hit net zero carbon emissions by 2050. The changes required are huge in terms of the way our buildings will be heated, the cars we will drive and generally how both businesses and the energy grid will operate. And, these changes will need to start now if we have any chance of achieving our target.

As such, the decarbonisation commitments from the private and public sector will be absolutely crucial to our net zero success, and many organisations have already set ambitious targets for reducing carbon emissions across their operations.

However, this does not come without its challenges. When we are working with organisations on their decarbonisation strategies, one of the most common questions we are asked is, 'how much will this cost?'. At a time when competition for capital expenditure (CAPEX) is particularly tough as businesses navigate a period of major recovery, making the case for investment in energy efficiency and larger decarbonisation measures can be challenging. In our previous report - 'Plot Your Path to Net Zero: A Focus on Sustainable On-Site Generation' - one of the primary barriers to investment was securing funding.

Added to this, at the time of writing, we are still awaiting guidance from HM Treasury on how the UK's net zero ambition will be funded. In its forthcoming Net Zero Review, we are expecting details of the contribution businesses will be expected to make. Last year, our 'Your Business Blueprint - The Road to Net Zero' report revealed concerns from organisations about the potential economic impact on their business of funding the transition.

There was also a difference in opinion as to who should fund the majority of the transition - when asked to rank who should bear the cost, respondents were split between the government and large energy intensive industries, with financial institutions also ranking highly.

That said, there was an acknowledgement that there would be an obligation on businesses to contribute, so in this report, we have revisited the theme of funding net zero, to see if these views have changed following the publication of the Energy White Paper in December 2020 and the Industrial Decarbonisation Strategy in March 2021. We also examine the funding strategies and options available to organisations, as well as provide practical advice on how to make the business case for investment in low-carbon measures when budgets are tight.

We hope you find it useful.

Anthony Ainsworth

COO, I&C Energy Sales and Solutions,
E.ON UK and npower Business Solutions (nBS)

Executive summary

We consulted with more than 60 businesses across areas including manufacturing, transport and the public sector to find out how they fund sustainability projects, who should bear the most responsibility for funding the net zero transition, and whether they believe the existing government policies go far enough to encourage investment.

Businesses use their own finance to fund projects, and recognise the importance of doing so

The majority (67%) of organisations we spoke to use funds from within their business to finance energy efficiency and sustainability projects, and for many, achieving net zero will require them to invest up to 15% of their annual turnover. That said, despite the potential significant cost, the majority of businesses believed that the climate benefits outweighed the cost impact.

Businesses are concerned about the cost impact of funding net zero

With the government's interim Net Zero Review stating that the transition to net zero will require new investment from business and that 'these costs are primarily capital expenditures', 70% of our respondents said they were very or slightly concerned about the potential cost to their business.

In terms of who should contribute the majority of the funding for the net zero transition, our respondents believe that large, energy intensive users and the government should foot the bill. A large number of businesses also said that financial institutions will play a key role.

Current government policy does not go far enough to support businesses

Our findings show that more support and certainty is needed from the government to help businesses make the necessary changes to their operations. When asked whether they felt the most recent government policies and strategies offer enough incentives for businesses to invest in decarbonisation measures, 75% of our respondents said no.

Investigating alternative ways to fund capital projects, such as government grants or other finance options, could help to reduce the financial burden of the low-carbon transition.

Section 01

Funding net zero: what are businesses doing?

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Funding net zero: what are businesses doing?

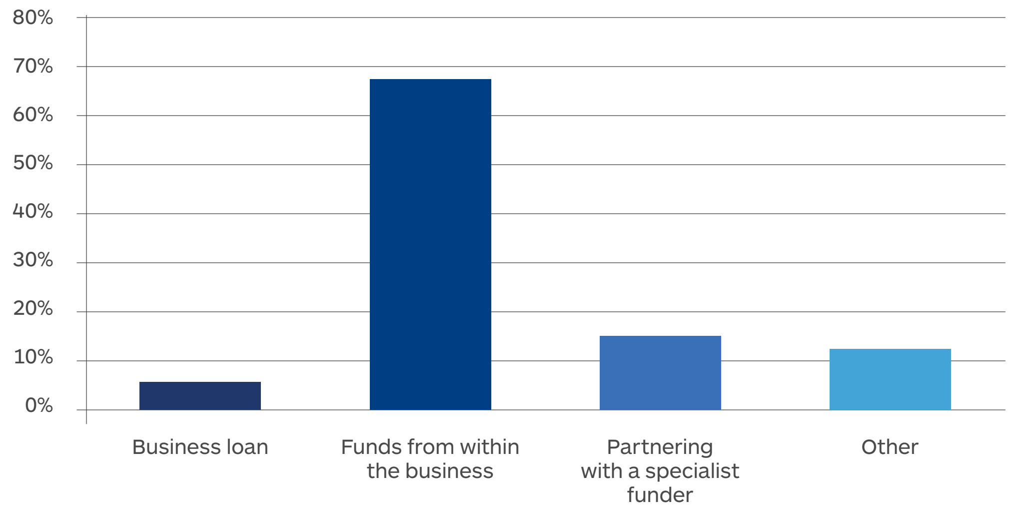
When it comes to financing energy efficiency and sustainability projects, the majority (67%) of organisations we spoke to use funds from within their business, with a smaller number choosing to partner with a specialist funder and very few choosing to take out a business loan. (Figure 1.)

Other answers revealed that some businesses had been successful in securing additional funding via grants from external organisations including Innovate UK and the Department for Business, Energy and Industrial Strategy (BEIS).

Some respondents said that a combination of grants, loans and money from within the business had allowed them to invest and, interestingly, one respondent was able to secure €2 million in European Commission (EC) grants 'owing to the lack of UK grants' available.

For on-site generation, Power Purchase Agreements (PPAs) were mentioned and some of the respondents from public sector organisations had accessed funding from the Public Sector Decarbonisation Scheme (PSDS).

Figure 1: How would your business usually fund capital investment energy/sustainability projects?



When asked about how much of their annual turnover businesses predicted they would need to allocate to fund their sustainability ambitions, the answers revealed that 70% felt it could be up to 15%, while one in six (16%) believed that this could be as much as 20%. Some anticipated it would cost even more to hit the net zero timelines set out by the government. (Figure 2.)

That said, the majority of organisations (72%) were in agreement that the climate benefits of funding their decarbonisation plans outweigh the potential cost impact. (Figure 3.)

This demonstrates that they support the net zero ambition and understand the positive long-term impact on their organisation in terms of both reducing emissions and costs.

Figure 2: How much of your annual turnover do you think you will need to invest to put measures in place to decarbonise your organisation?

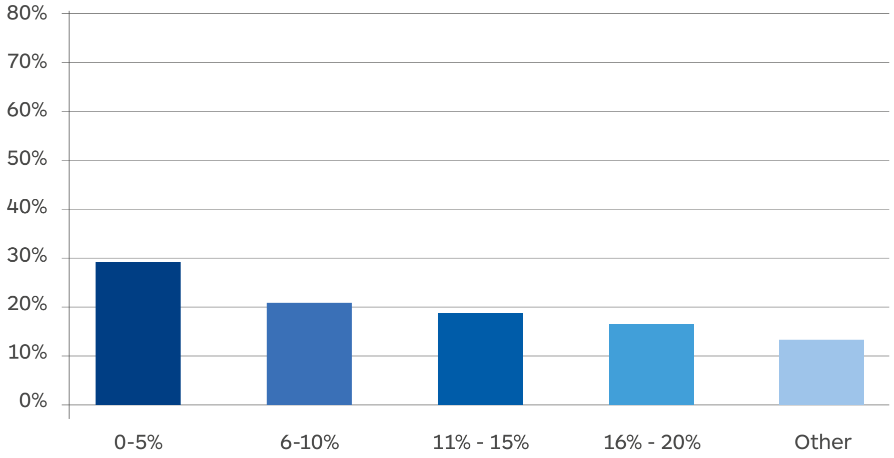
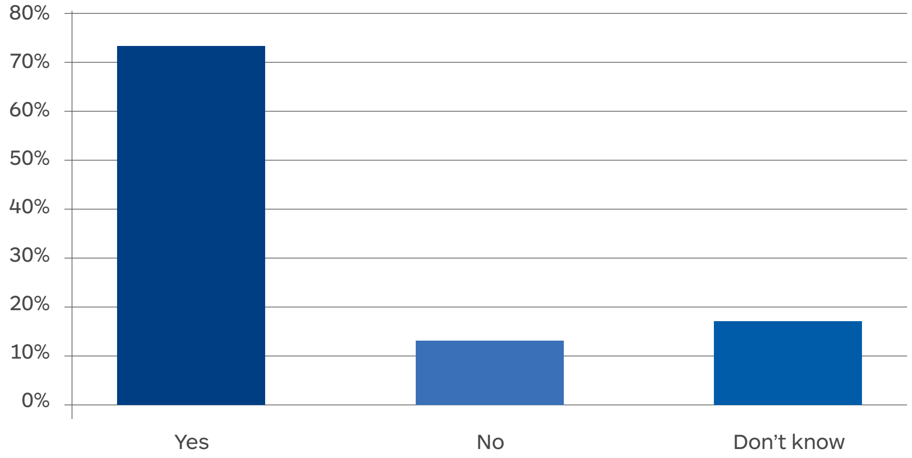
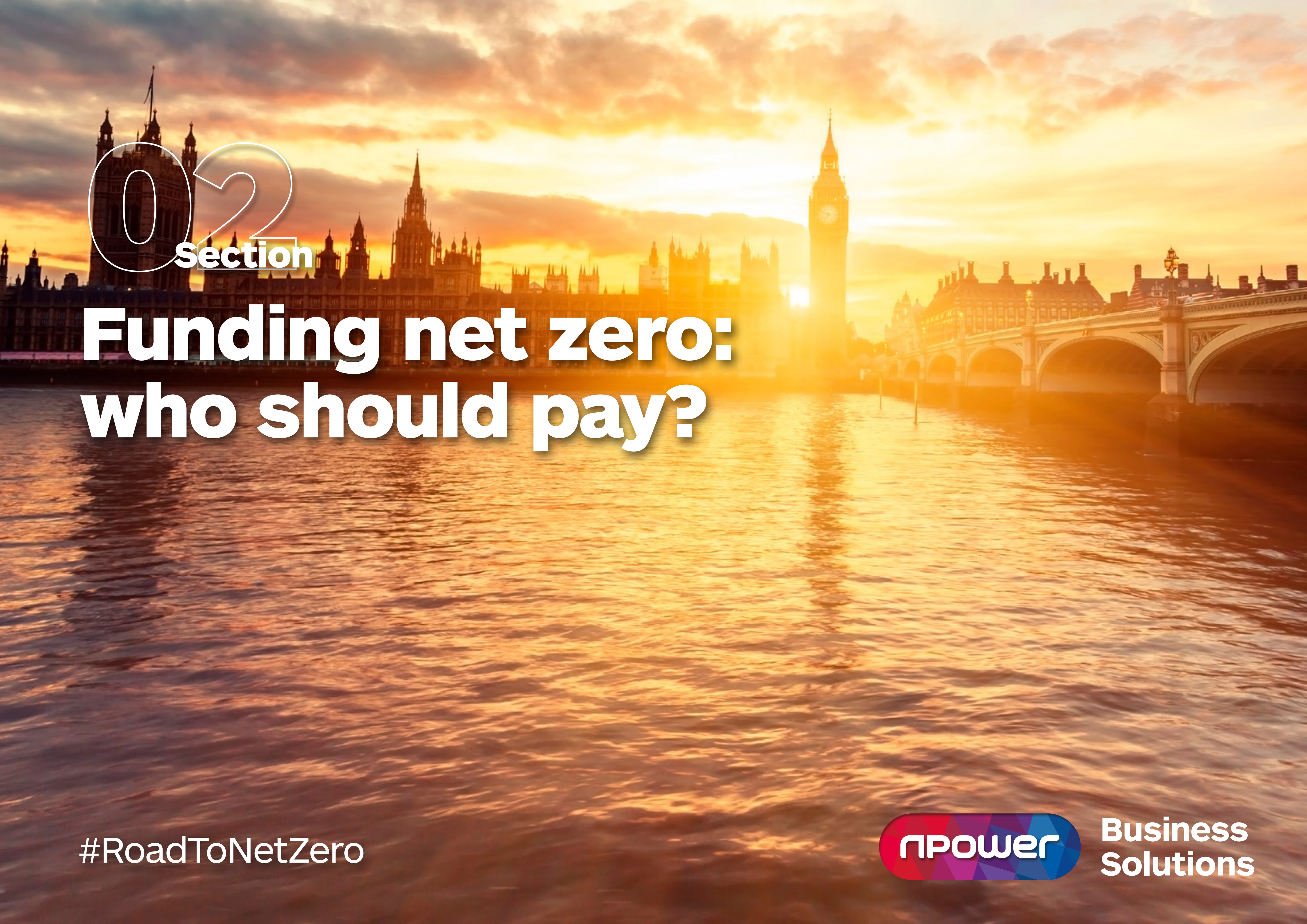


Figure 3: Do you believe the climate benefits of funding net zero outweigh the potential cost impact?





02 Section

Funding net zero: who should pay?

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Funding net zero: who should pay?

In its interim Net Zero Review, published in December 2020, HM Treasury said that: “Reaching net zero will be a collective effort across households, businesses and the government.” The report contained initial analysis, rather than firm policy recommendations, ahead of the publication of the Review’s final report, which is expected imminently in 2021.

What is clear from the report is that transition to net zero requires new investment and that ‘these costs are primarily capital expenditures, but will also encompass changes to the long-term operating costs of the economy.’

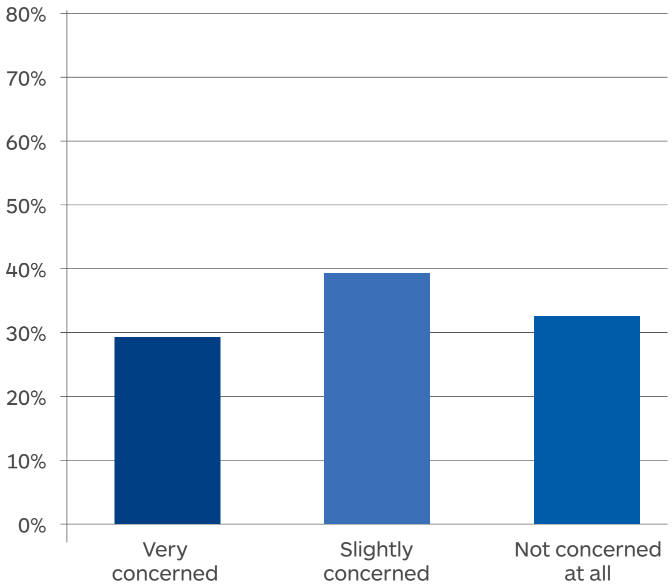
While the scale of the investment will differ from business to business, the report says that ‘the net impact will depend on the business’s current carbon exposure and their ability to change consumption patterns or business processes.’ For example, how businesses make their buildings more efficient will be key, as will replacing petrol or diesel cars with electric vehicles (EVs).

It also said that areas to take into account included the ‘timing of natural investment cycles, the rate at which technology costs fall, innovation and nationwide system-level decisions, such as the choice of energy mix over the next decade.’[1]

As mentioned earlier, in our 2020 report - ‘Your Business Blueprint - The Road to Net Zero’ - 46% of businesses expressed concern about the potential impact of funding the low-carbon transition on their organisation.

In our latest feedback, this has grown, with 40% saying they were slightly concerned, and a further 30% saying they were very concerned. (Figure 4.)

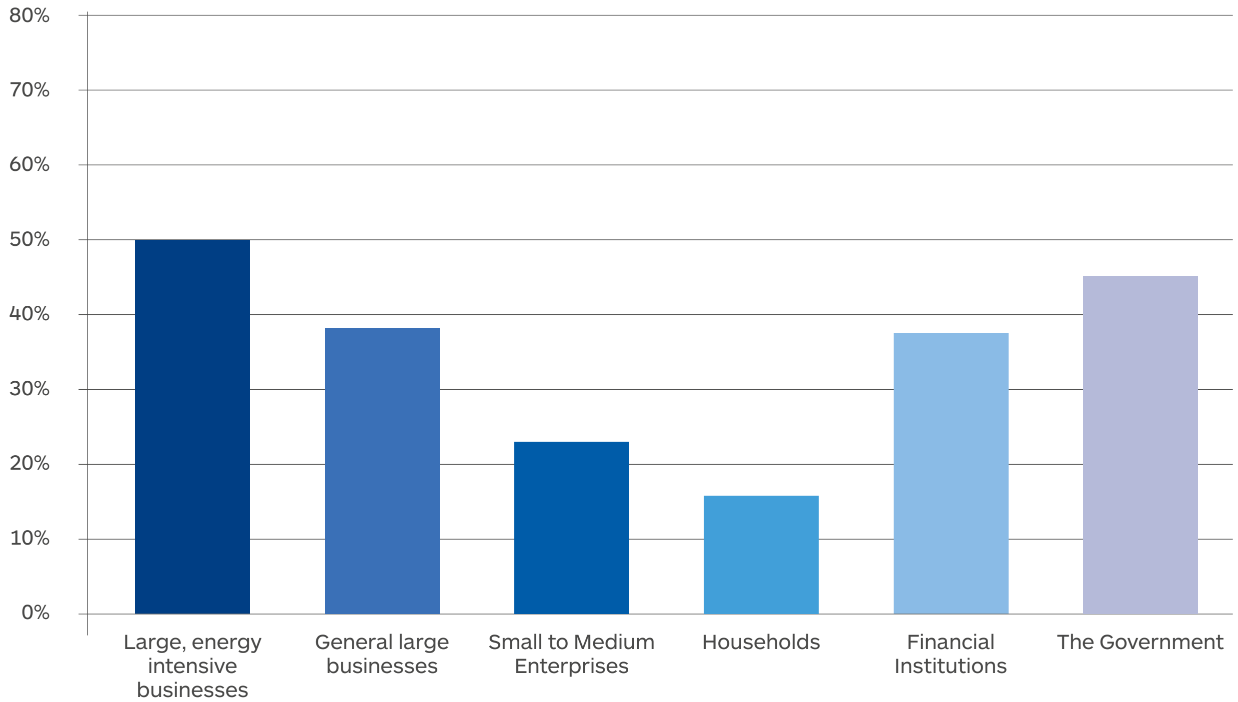
Figure 5: How concerned are you about the potential additional cost to your business to fund the net zero transition?



1 assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945827/Net_Zero_Review_interim_report.pdf

Opinions on who should contribute the majority of the funding towards the net zero transition haven't changed since we last consulted with businesses, with the vote still split between large, energy intensive businesses and the government. (Figure 5.)

Figure 5: Which group do you believe should contribute the majority of funding for the net zero transition?



Interestingly, for this report we also asked a further question about whether financial institutions will play a vital role in supporting businesses by helping to fund the net zero transition. As indicated in 'Figure 6', the overwhelming majority (82%) either strongly agreed or agreed that this was the case.

With this in mind, in the March 2021 Budget, the Chancellor of the Exchequer confirmed a new National Infrastructure Bank - which was recently launched in Leeds - and that its primary focus will be on investment in public and private green projects. The Bank will have an initial £12 billion capitalisation.

We asked our respondents whether they thought this would be enough to spur the necessary investment needed for low-carbon measures. As 'Figure 7' shows, while just over one fifth (22%) thought it would, 44% thought it wouldn't go far enough.

Figure 6: To what extent do you agree with the following statement: "financial institutions will play a crucial role in funding the net zero transition"?

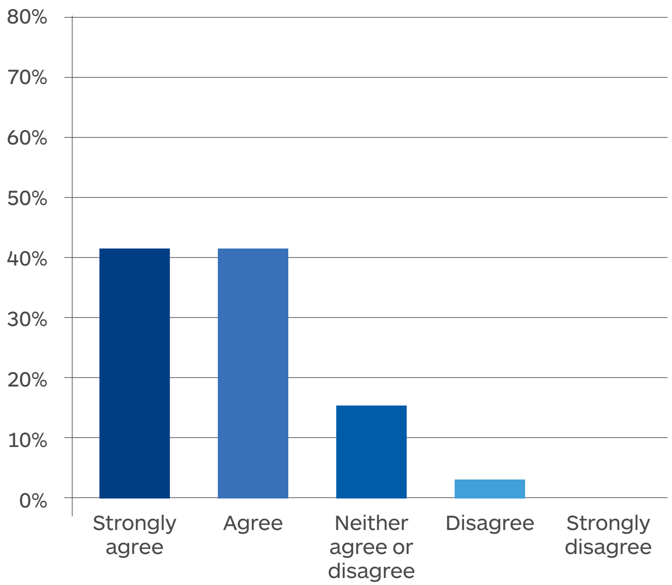
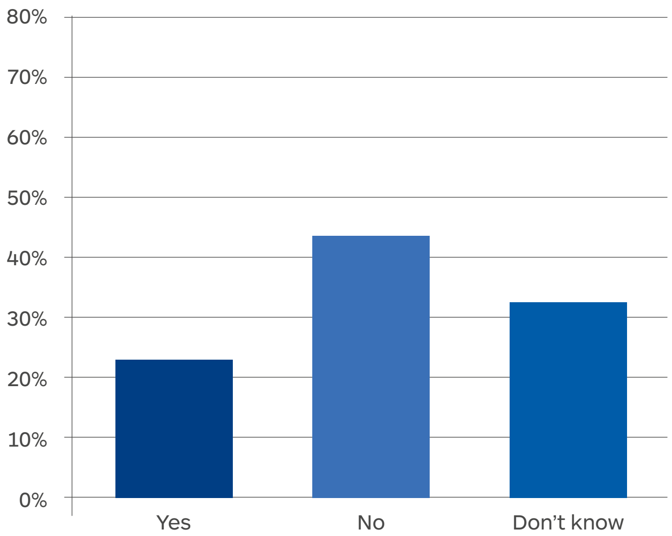


Figure 7: Do you believe the National Infrastructure Bank's initial £12 billion capitalisation is enough to spur investment from organisations in low-carbon measures?



03

Section

Funding net zero: options for businesses

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Funding net zero: options for businesses

As outlined earlier in this report, the majority of businesses use their own funds to finance energy efficiency and low-carbon projects. As expected, the amount varies from business to business, with some anticipating they will need to spend in excess of 15% of their annual turnover to decarbonise their operations.

During a time of economic uncertainty, investigating alternative ways to fund capital projects - such as government grants or other finance options - could provide some welcome relief and reduce the financial burden of the low-carbon transition.

That said, our findings show that more support and certainty is needed from the government to help businesses make the necessary changes to their operations. When asked whether they felt the most recent government policies and strategies - including the Ten Point Plan, Energy White Paper and Industrial Decarbonisation Strategy - offer enough incentives for businesses to invest in decarbonisation measures - most of our respondents said no.

So, what are the current funding options available to businesses if securing CAPEX is challenging?

Industrial Energy Transformation Fund

While the government has announced funding to support the development of major new technologies that will help decarbonise industry in the longer term, such as carbon capture, utilisation and storage (CCUS) and low-carbon hydrogen production, there are also existing schemes some businesses may be eligible for now.

In fact, the government says it has £5 billion of funding available to help UK businesses become greener and to support their net zero journeys. These include the Industrial Energy Transformation Fund, which is a £289 million fund to help energy intensive businesses to cut their energy invoices and carbon emissions by investing in energy efficiency and low-carbon technologies.

Eligibility for government schemes will vary depending on the business's size and sector - you can check if your organisation is eligible for the latest schemes here.

Green Heat Network Fund (GHNF) Transition Scheme

Recently announced by BEIS, the GHNF is a capital grant fund open to public, private, and third sector applicants in England. It will build on the progress made by the Heat Network Investment Project (HNIP), by supporting the development of low and zero carbon heat networks (including the supply of cooling).

The purpose of the transition scheme will be to better ensure that low-carbon heat network projects are construction-ready in time to apply to the GHNF full scheme when it opens for applications in the next financial year (April 2022 - March 2023).

The GHNF Transition Scheme will open to funding applications on 5 July 2021 and offer commercialisation funding only.

The Public Sector Decarbonisation Scheme (PSDS)

The Industrial Decarbonisation Strategy, published in March 2021, confirmed a second round of funding for decarbonisation projects across England through the PSDS. The aim of this is to reduce carbon emissions from public buildings, and many local authorities, NHS Trusts and other public sector organisations benefited from Phase 1 of the scheme, using funds to install measures to make their properties more efficient.

Salix Finance Ltd - which is a non-departmental public body, wholly owned by the government - is currently delivering all allocated funding for Phases 1 and 2 of the PSDS.

Power Purchase Agreements (PPAs)

PPAs are a popular way of financing on-site generation projects, such as solar photovoltaic (PV) or wind, when securing up front capital is an issue. They are a long-term agreement where a third party funder installs and manages the on-site asset and the organisation then buys the energy from the funder over the course of a long-term supply contract, negating the need for up front investment.

If suitability for on-site generation at a particular site is also an issue, businesses can still benefit from a PPA to purchase energy from a local renewable energy source.

Local authority energy efficiency schemes

For non-industrial or less energy intensive businesses, there are other potential options to secure grants for energy efficiency projects. For example, many local authorities operate energy efficiency schemes to help fund measures for smaller businesses - a useful roundup can be found here.

Finding the right option for your organisation

We have outlined just some of the options available to organisations. There are also flexible funding models for certain types of projects, just speak to your energy partner about what you would like to achieve and they can help you with a funding option that is right for your business.

Section 04

The expert view: making the business case for net zero investment

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The expert view: making the business case for net zero investment

David Baker, Development Manager, I&C Energy Solutions, E.ON UK and npower Business Solutions (nBS)

As we've examined in this report, organisations overwhelmingly support the role they will need to play in the UK's net zero ambition. However, concerns around releasing capital to fund projects - particularly during times of economic uncertainty - mean that sustainability initiatives could be put on hold if more pressing financial needs are identified.

That said, while 2050 may seem a long way off, significant action needs to be taken now to have the necessary impact so we can achieve our ambitious carbon reduction targets.

So, how can organisations make the business case for net zero investment? For us, there are four key areas to focus on:

Small changes can make a big difference

When it comes to energy efficiency and low-carbon investment, there is often the misconception that it will immediately require major capital expenditure. This is not always the case as 'quick wins' such as switching to more efficient lighting, air conditioning and heating can result in significant energy savings without much upfront cost.

An energy audit will be able to identify where some of the most effective low-cost, relatively small changes can be made to result in maximum savings - savings that can then be redirected into further sustainability measures. Energy efficiency really is a 'no regrets' action and can be implemented relatively quickly.

Demonstrate return on investment (ROI)

For larger projects that require greater amounts of funding, such as installing an energy management system or an on-site asset, it is important to demonstrate the short, medium and long-term benefits it will bring to the business. For example, depending on the project, these could include:

- Reduction in carbon emissions
- Reduction in energy invoices
- Improved reputation
- Greater employee engagement
- Higher self-sufficiency i.e. less reliance on the grid
- Opportunity for additional revenue streams, for example via Demand Side Response (DSR)

Having either real-life examples or robust data modelling to show the potential positive impact of a project is key to securing investment.

Explore additional funding options

As outlined earlier in this report, it is important to do your research as to what additional funding options are available before you commit to a project, as it may be your business is eligible for government funding or a local authority grant, particularly if you work in an energy intensive sector.

Similarly, PPAs can help fund on-site generation with minimal financial risk, and there are also flexible funding options available for businesses that may want to switch from a PPA to owning an asset during the PPA's term - just speak to your energy partner to see what the opportunities are for your organisation.

Showcase results

If you have secured funding for a sustainability project, it is vital to demonstrate the results as this will help unlock further investment for future initiatives.

This is where good data management is crucial to understand how the measures are performing and to enable you to identify improvements. These could include looking at how adapting times of use, the efficiency of infrastructure and processes, and changing employee behaviour can impact the success of a project. It will also help you to demonstrate a clear ROI in terms of reducing emissions and costs.

How we can help

However ambitious your sustainability goals are, our business energy experts can help your organisation to make the case for net zero investment.

Contact us

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