

Renewable energy: Standing on its own two feet

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Government subsidies helped make wind and solar the cheap sources of energy they are today - cheap enough to now compete without the prop that subsidies provide.

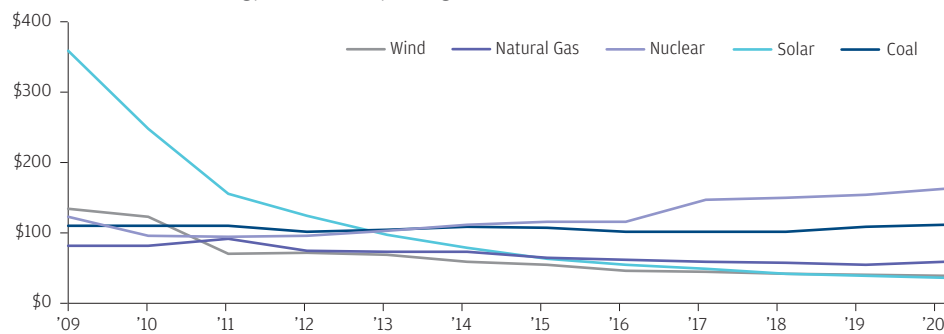
The energy sector has come a long way in its battle to decarbonise the world. Crucially, the cost of renewables has dropped fast. For example, 10 years ago the power price needed to make a new solar power station economically viable was four times that of a gas plant. Now, however, across the world solar and wind are the cheapest ways to meet new power demand or make up a shortfall caused by shutting coal plants.

We have made progress so far through private-sector know-how and strong policy incentives, including renewables subsidies. Without subsidies, the private sector may not have had the time and resources to get wind and solar capacity up and running, and then plough research & development spending into making these energy sources ever more cost-efficient.

Because of this support, renewables can now more than hold their own without subsidies.

EXHIBIT 1: RENEWABLE ENERGY COSTS HAVE DECLINED SUBSTANTIALLY

Cost of wind, solar, natural gas and coal
Mean levelised cost of energy, 2020, dollar per megawatt hour



Source: Bloomberg, Lazard, Eurostat, METI, BP Statistical, J.P. Morgan Asset Management. Levelised cost of energy represents the net present value of the unit-cost of electricity over the lifetime of a generating asset. It is often taken as a proxy for the average price that the generating asset must receive in a market to break even over its lifetime. Guide to Alternatives. Data as of 28 February 2021.

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Policy will therefore not be as essential as before, in driving decarbonisation. However, it will still be helpful.

May 2021 gave us a case in point. The Dutch government paid €2 billion in subsidies to a consortium including Royal Dutch Shell and ExxonMobil for a carbon capture and storage (CCS) project. The plan is to take carbon produced by the port of Rotterdam and the large industrial complex around it – carbon generated by burning fossil fuels – and store it in empty gas fields. Many experts believe that subsidies will eventually make CCS profitable in the free market.

PORTFOLIO INSIGHTS

GETTING OUT OF THE WAY

Do not underestimate the importance of the opposite approach to subsidies: simply getting out of the way. Over the past 20 years, the utilities sector has suffered frequent raids from governments during economic downturns, when they needed extra tax revenue. The European Union's Green Deal removes this risk in much of Europe by making billions of euros available to member states, contingent on investment from the utility companies to boost the share of renewables in their energy mix. After bidding for this money, national governments cannot then tax their utilities so heavily that they are unable to invest in renewables after all. In the US, meanwhile, the Biden administration has adopted its own ambitious set of proposals to decarbonise America. These include clean energy tax credits, but legal and regulatory obligations to accelerate the use of renewables will also be important – in the US and elsewhere.

For example, under a climate law adopted by Germany in May, the country must raise wind and solar's share of electricity production from 43% now to 65% by 2030.

CONCLUSION

The renewables sector needs less government support than in the past, because it is now highly competitive on price. For this reason, government policy to support renewables will be less essential – but it will still have some use in encouraging new decarbonisation technologies.

NEXT STEPS

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