From Discontent to UK Content

7 October 2015

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BVGassociates

About BVG Associates

BVG Associates

- Market and supply chain
  - Analysis and forecasting
  - Strategic advice
  - Business and supply chain development
- Economics
  - Socioeconomics and local benefits
  - Technology and project economic modelling
  - Policy and local content assessment
- Technology
  - Engineering services
  - Due diligence
  - Strategy and R&D support

Selected clients

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I’m going to talk about …

… the weather

From discontent … to glorious summer

- Why we are here
- How and where UK content will be used
- The reporting framework – how it works
- The data gathering methodology
- The controversial bit
- Concluding thoughts

Why we are here

Once a "target" has been announced, DECC realised that there needed to be a way of measuring

Significant shift from emphasis on deployment to securing economic benefit (with lower cost of)

- Deployment and building an industry was a key objective early on – openness of the UK market one of its attractions.
- There is political pressure on all major infrastructure projects - the wind industry is not unique.
- There are different measures of economic benefit – it's ultimately about jobs
- Tends to be ambiguity about job forecasts – they always seem suspiciously high

A challenge for civil servants

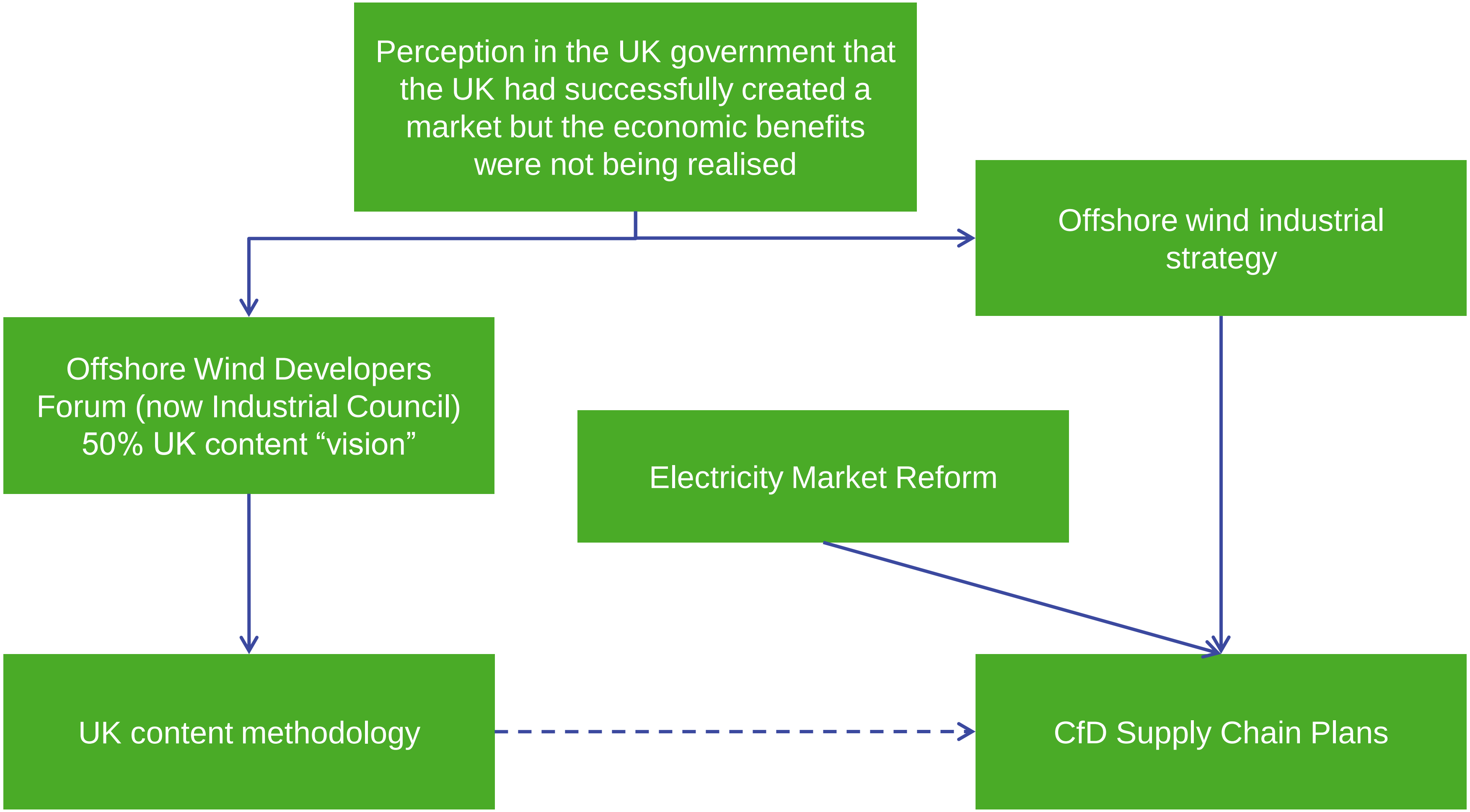
- At its meeting on 6 February 2012, the Offshore Wind Developers Forum (OWDF) (now reconstituted as the Offshore Wind Industry Council) agreed to publish a vision for:

"The UK to be the centre for offshore wind technology and deployment, with a competitive supply chain in the UK, providing over 50% of the content of offshore wind farm projects"

- But what does it mean and how do you measure it?
    - 50% of what?
    - How to you calculate it?
    - How is data gathered and reported?
- DECC, Crown Estate and RUK asked BVGA to come up with a method
- Industry should take great credit for adopting a formal and consistent process for measuring it.

How and where UK content will be used

The UK content methodology and supply chain plans are distinct but related initiatives

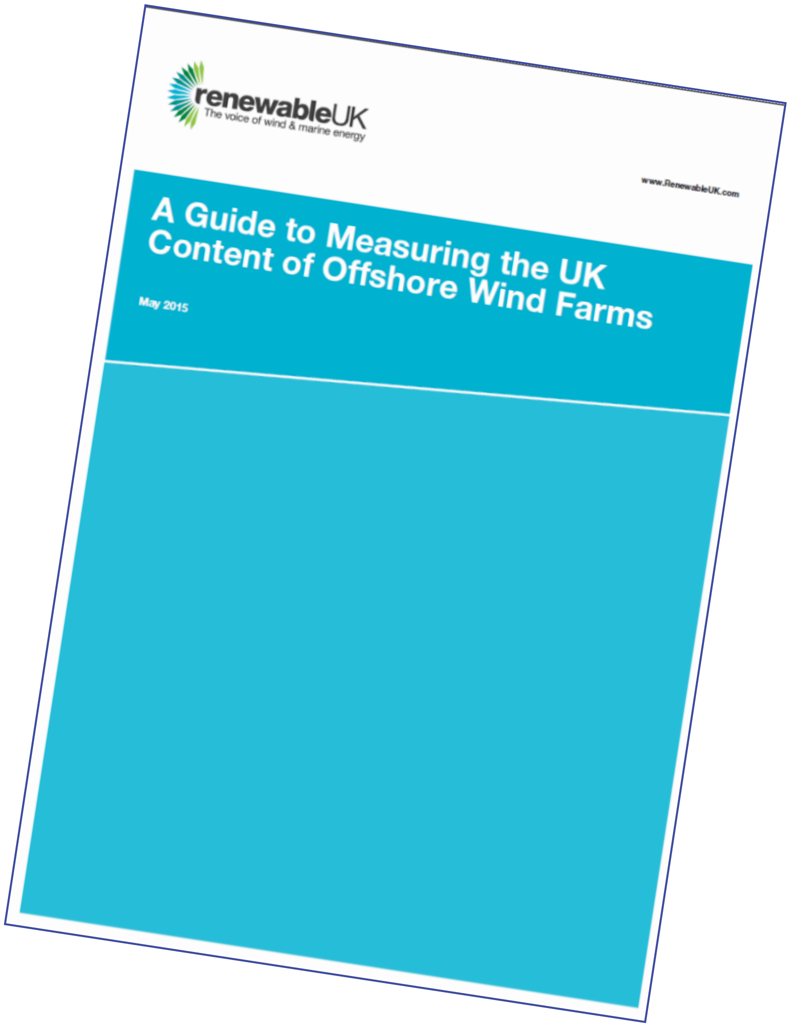


The reporting framework

RenewableUK has taken on the job of gathering and publishing the data

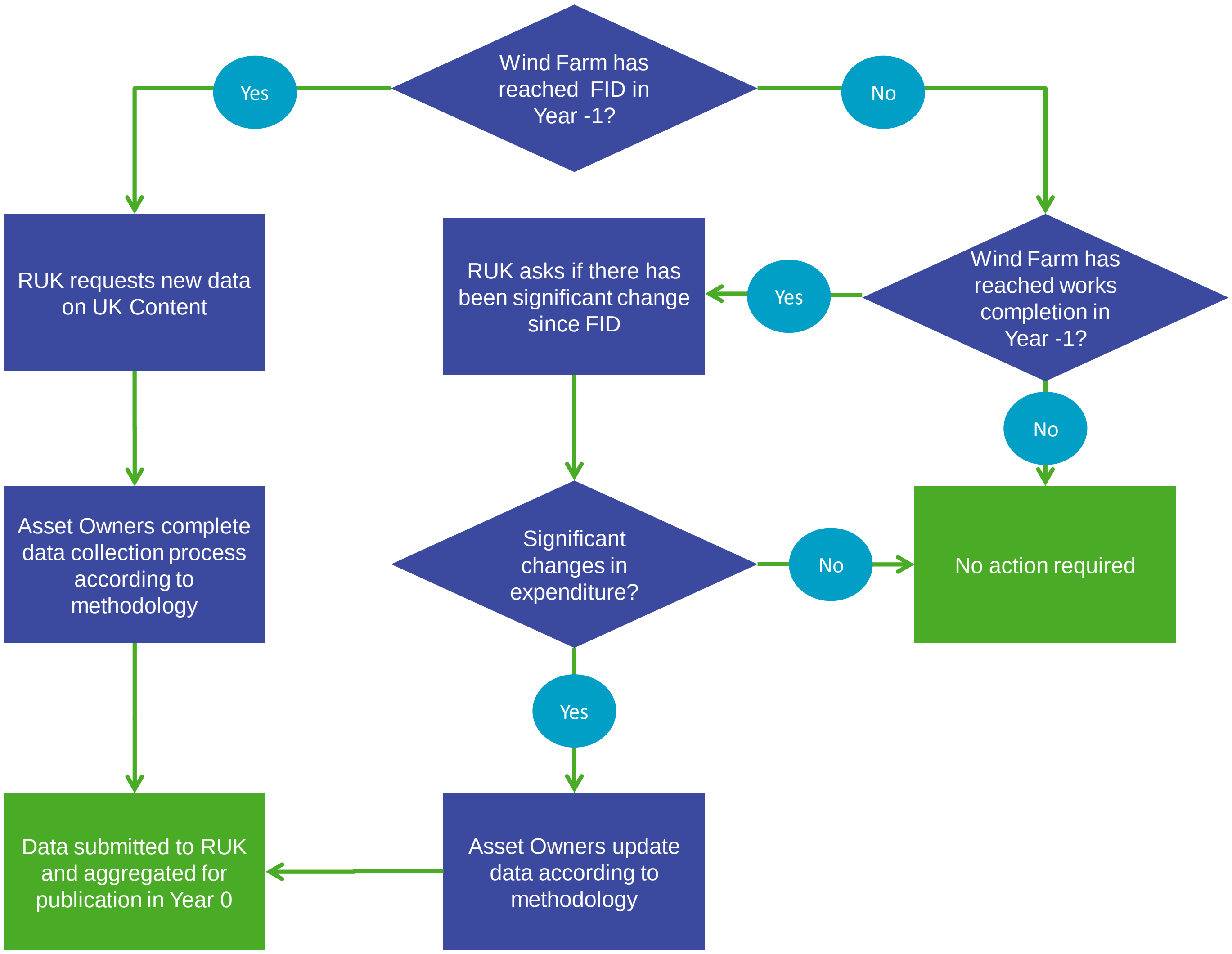
Aim has been to minimise the amount of data needed

- Process ‘live’ from January 2015
- Four figures (percentages only) will be published for UK content:
    - UK content in DEVEX
    - UK content in CAPEX
    - UK content in OPEX (undiscounted)
    - UK content in TOTEX (total expenditure)
- Option to provide more detailed data – subdivided into about 20 categories.
- Data published as a rolling five year average



RenewableUK reporting framework – how it works

There will be an annual cycle



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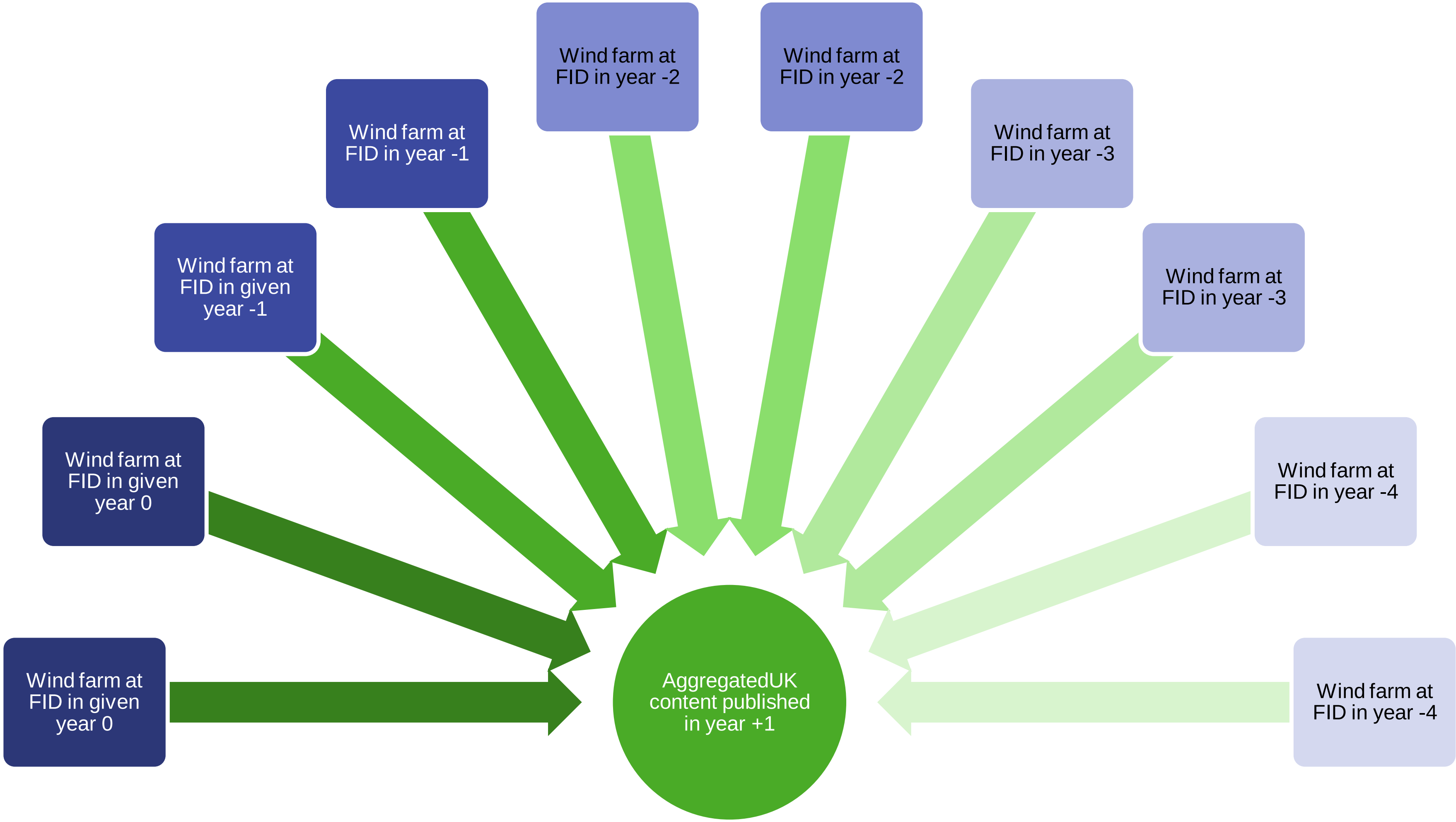
RenewableUK reporting framework – data aggregation

Data from different wind farms will be weighted by generating capacity



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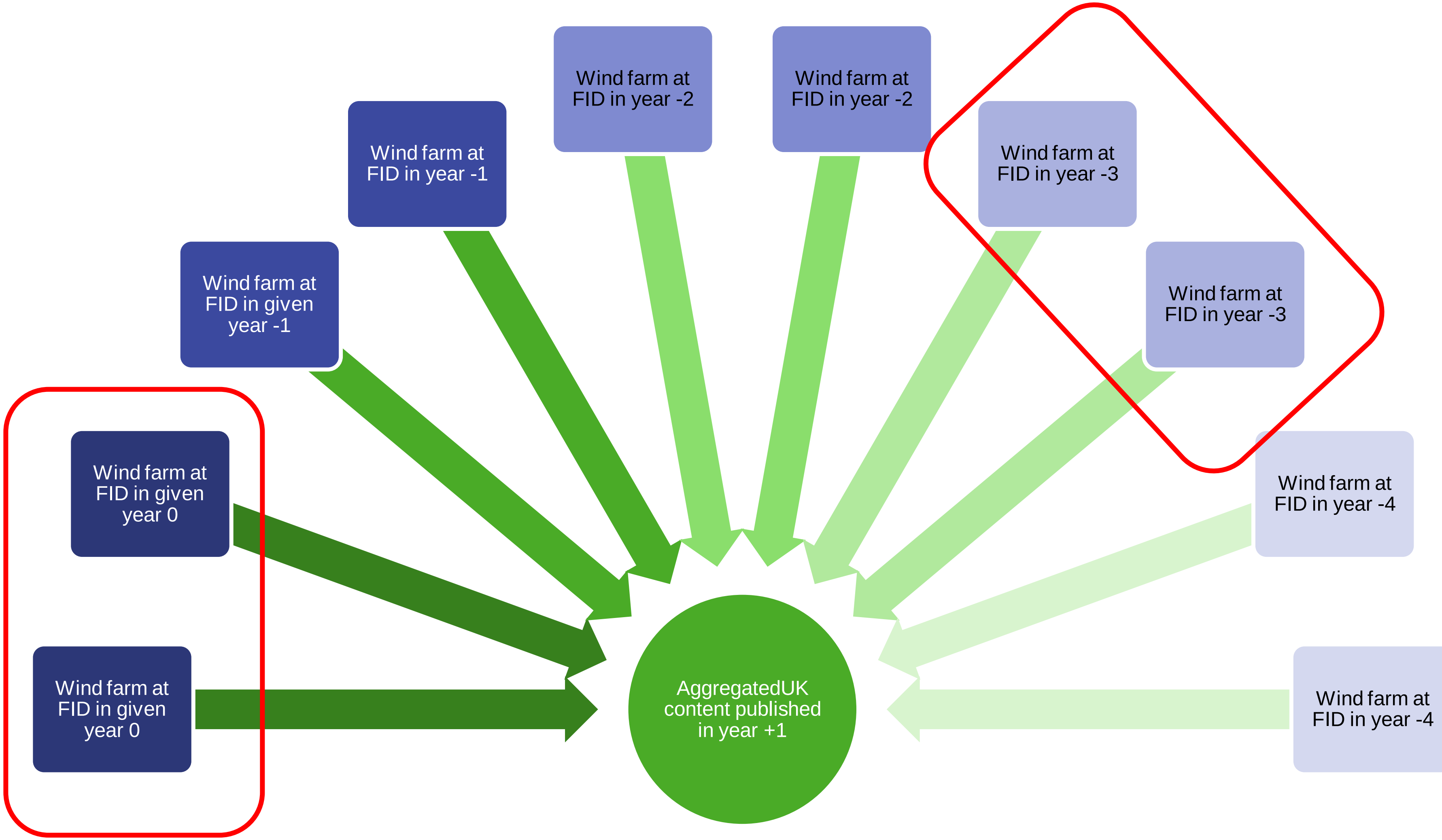


Methodology overview

Ready to go after three years in discussion

The document's coverage

- Definitions
- Scope
- Rules
- How to gather data – with specific guidance
- Principles
  - Simple
  - Clear
  - Consistent
  - Minimal burden
  - Respect commercial confidentiality
- No-one has to say how much profit was made or how much was paid to subsuppliers
- Tried to formalise "common sense"

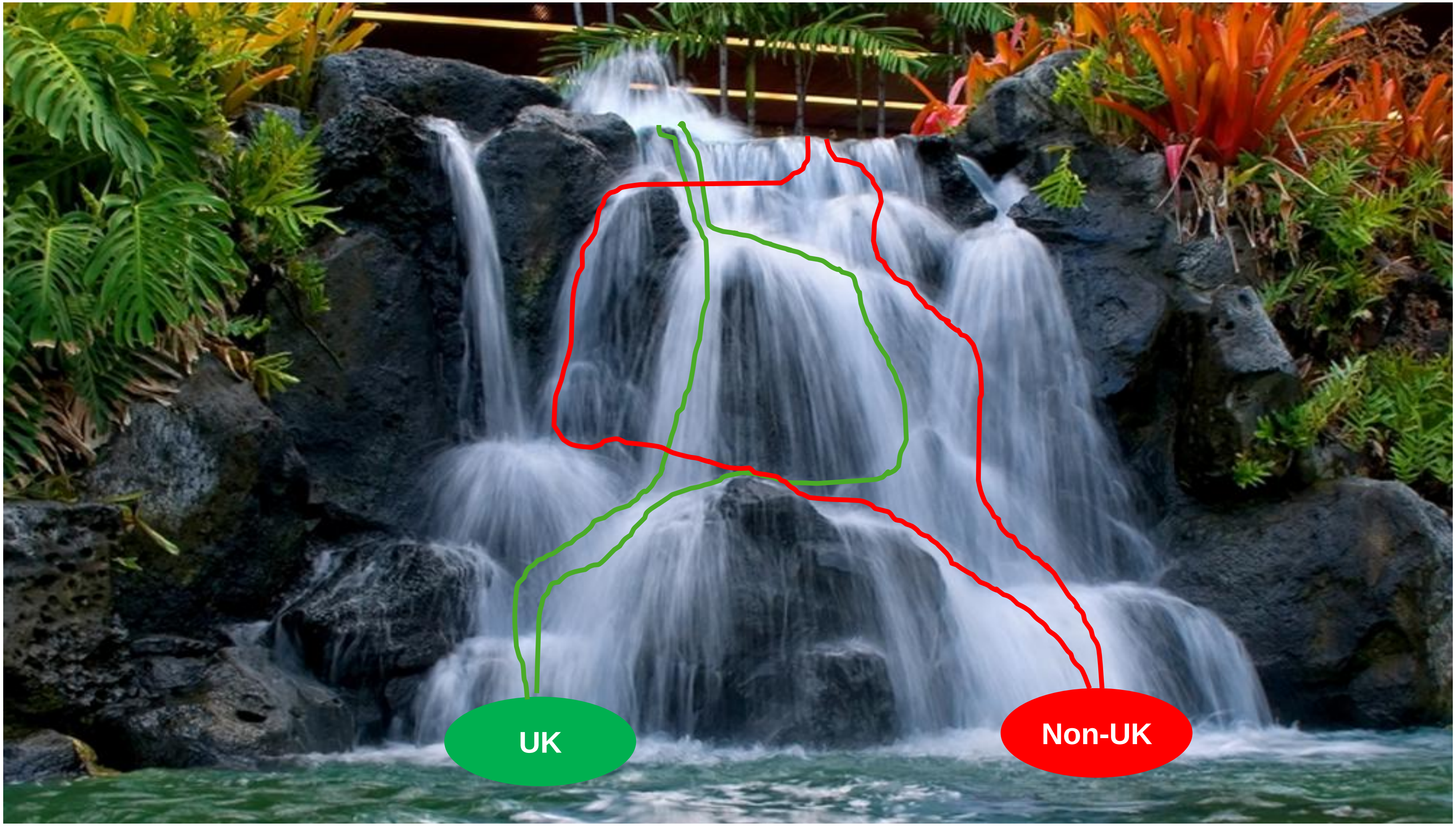
Key definitions

Clarity is vital to the methodology

Wind Farm	Has the following attributes: • It is developed through a single leasing option awarded by The Crown Estate. • It has two parts: the Generation Asset and the Transmission Asset • It has a discrete final investment decision (FID), procurement process and construction phase
Wind Farm Asset Owner	The company that owns either the Wind Farm Generation Asset (the Generation Asset Owner) or the Transmission Asset (the offshore transmission owner (OFTO)) during development, construction or operation
Customer	A purchaser of Products for the Wind Farm, which may be a Wind Farm Asset Owner or a Supplier at any tier of the supply chain (except the bottom tier)
Supplier	A provider of products to a Customer. A Subsupplier is a company that is two or more steps down the supply chain from the Customer. A tier 1 Supplier is one that is directly Contracted by the Wind Farm Asset Owner.
Contract	An agreement between a Customer and a Supplier to provide a Product for an agreed value. It covers the aggregated payment by the Customer in DEVEX, CAPEX or OPEX to the Supplier. The Contract value could therefore be made up of a number of transactions. A Contract may be between a Customer and an <u>external</u> or <u>internal</u> Supplier.
UK Content	The %age of the total undiscounted expenditure by the Wind Farm Asset Owner on a Wind Farm that is ultimately spent through Contracts awarded to companies operating in the UK.

A UK content metaphor

To make the presentation less dry



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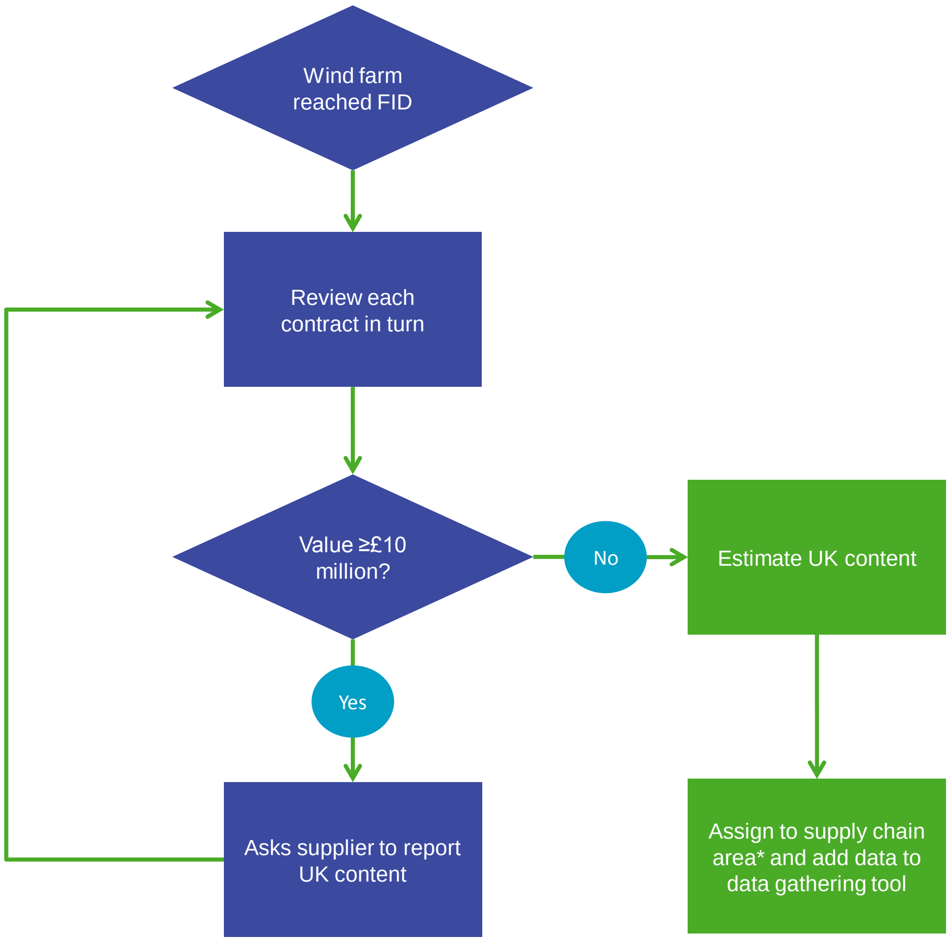
The process

Process starts with the developer

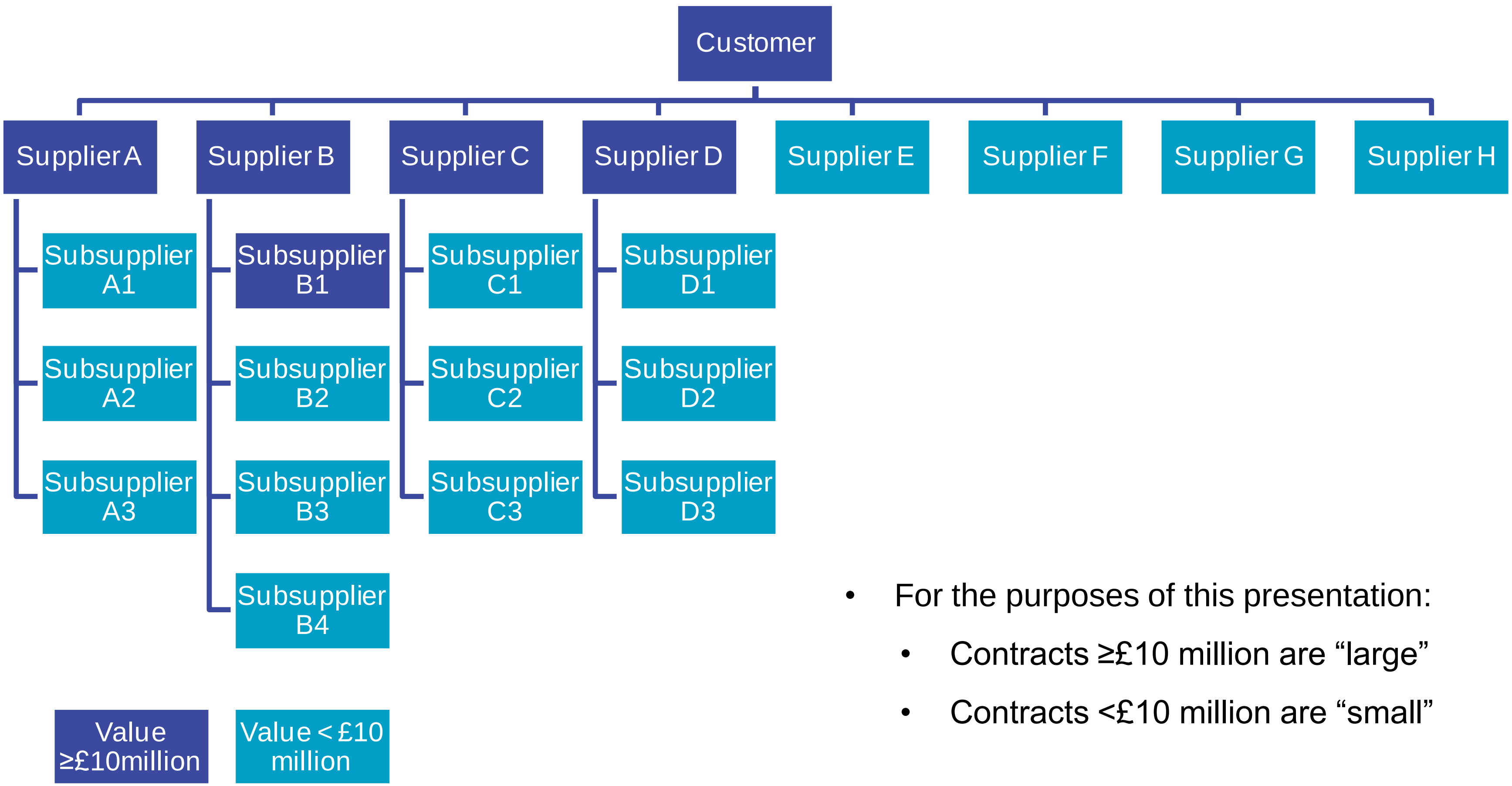


UK content is ultimately estimated for all spend

- Contracts less than £10 million? Make an estimate based on:
  - Any information provided by the Supplier
  - The invoice address of the Supplier
  - The currency in which the payment was made
  - The Customer's knowledge of its Supplier's activities and Subsuppliers
  - The Customer's knowledge of the activities and Subsuppliers of similar companies

A theoretical example

Expected that few companies below wind farm owner's tier 2s will need to report



- For the purposes of this presentation:
  - Contracts ≥£10 million are "large"
  - Contracts <£10 million are "small"

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A theoretical example

Supplier	Contract value (£million)	UK Content in Contract	% of base cost in Contract	Contribution of Supplier's Contract to UK Content	Subsupplier	Subcontract (£million)	% of base cost in Subcontract	UK Content in Subcontract
A	12	71%	15%	10.6%	A1	6	55%	*85%*
					A2	4	36%	*55%*
					A3	1	9%	*45%*
					Margin	1		
B	20	47%	25%	11.7%	B1	10	43%	*25%*
					B2	5	29%	*75%*
					B3	3	14%	*45%*
					B4	3	14%	*75%*
					Margin	-1		
C	15	32%	19%	6.1%	C1	7	52%	*25%*
					C2	4.5	33%	*50%*
					C3	2	15%	*20%*
					Margin	1.5		
D	11	22%	14%	2.9%	D1	4	45%	*40%*
					D2	3	33%	*5%*
					D3	2	22%	*10%*
					Margin	2		
E	8	*46%*	10%	4.6%				
F	7	*85%*	9%	7.4%				
G	4	*65%*	5%	3.3%				
H	3	*90%*	4%	3.4%				
Base cost	80							
Margin	20							
Total	**100**			**50.0%**				

Specific challenges

Two types of challenge: the UK content calculation and the attribution of cost to the wind farm

A supplier is awarded a contract and fulfils it with a number of subcontracts

- Large component - project sourced (could be a turbine)
- Large component - dual sourced (could be a foundation)
- Large component – framework (could be a cable)
- Large component – internal (could be a blade)
- Factory running costs
- Corporate overhead
- Factory or vessel investment
- R&D
- Transport and storage
- Rent

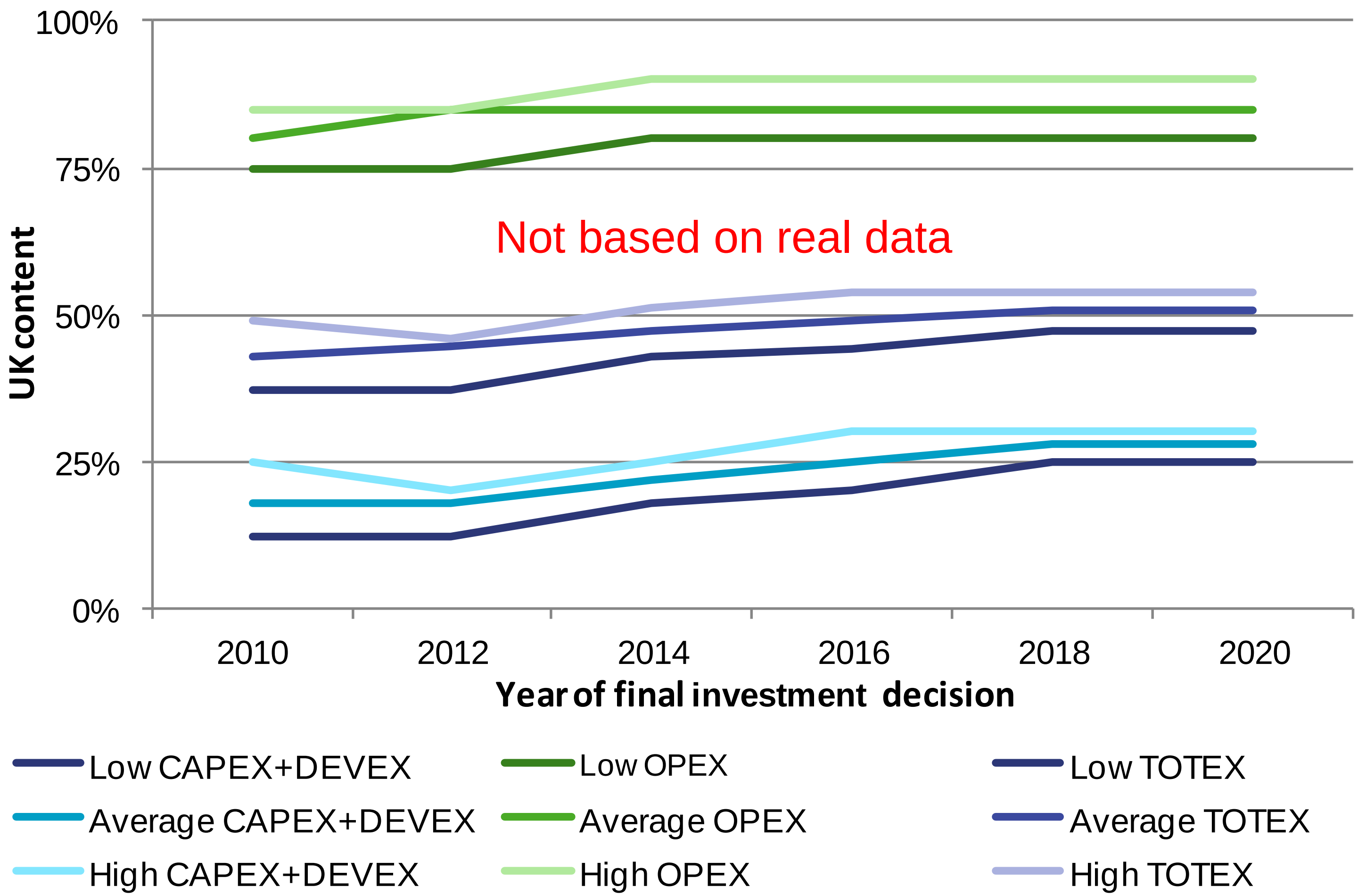
Small contracts

Assessment should be made based on a knowledge of the company

Type of Product	Examples	UK Content assumption for UK-based supplier
Desk-based services	Consultancy PR Legal Insurance	95%
Non-desk-based services using low-cost equipment likely to be imported	Electrical services Lifting services	70%
Non-desk-based services using high-cost equipment likely to be UK manufactured	Crew transfer vessels Transport	85%

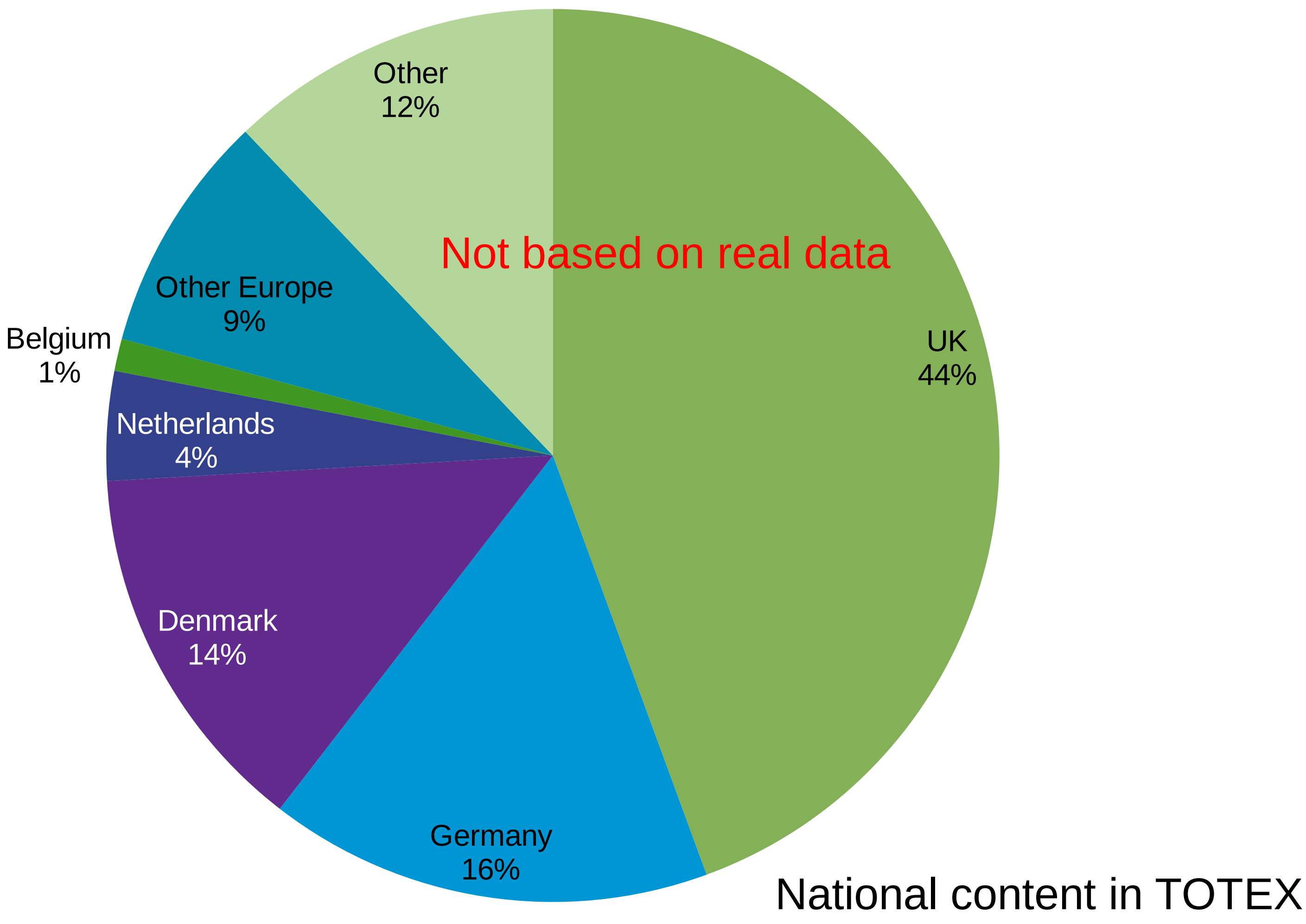
A vision realised?

UK investments will impact soon – but hard to see UK content rising without a bigger market



What about the non-UK content?

What if we looked at the origin of all components and services?



Concluding thoughts

- 50% UK content not far away – but there shouldn't be complacency
- Data published as a rolling five year average means that the impact of new UK investments will not be evident for several years – three years would be better
- Detailed data is only optional – it's not much more work and can help identify areas for action
- Everyone's job will be easier if companies spend a little time now getting prepared:
    - Talking with suppliers
    - Making data gathering tools
    - Briefing contract managers
- BVGA is always here to help