The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

ECONOMY, ENERGY AND TOURISM COMMITTEE

Wednesday 4 September 2013

Session 4

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ECONOMY, ENERGY AND TOURISM COMMITTEE
22nd Meeting 2013, Session 4

CONVENER

*Murdo Fraser (Mid Scotland and Fife) (Con)

DEPUTY CONVENER

*Dennis Robertson (Aberdeenshire West) (SNP)

COMMITTEE MEMBERS

*Marco Biagi (Edinburgh Central) (SNP)
*Chic Brodie (South Scotland) (SNP)
*Alison Johnstone (Lothian) (Green)
*Mike MacKenzie (Highlands and Islands) (SNP)
*Hanzala Malik (Glasgow) (Lab)
*Mark McDonald (Aberdeen Donside)
*Margaret McDougall (West Scotland) (Lab)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Rob Cormie (Green Investment Bank)
Shaun Kingsbury (Green Investment Bank)
Lord Smith of Kelvin (Green Investment Bank)

CLERK TO THE COMMITTEE

Stephen Imrie

LOCATION

Committee Room 4

Scottish Parliament

Economy, Energy and Tourism Committee

Wednesday 4 September 2013

[The Convener *opened the meeting at 10:00*]

Interests

The Convener (Murdo Fraser): Good morning, ladies and gentlemen, and welcome to the 22nd meeting in 2013 of the Economy, Energy and Tourism Committee. I welcome members back to Parliament after the summer recess, and I welcome our witnesses and I welcome the visitors in the gallery. I remind everyone to turn off—or at least to turn to silent—all electronic devices.

Two new members join us this morning. I welcome Mark McDonald and Hanzala Malik to the committee. I pay tribute to Rhoda Grant and David Torrance, who have left us, for their work on the committee and for their contributions to our debates. I ask the new committee members to declare any relevant interests.

Mark McDonald (Aberdeen Donside): Thank you, convener. I merely direct members to my entry in the register of interests, but I do not believe that I have any interests that are relevant to the committee.

Hanzala Malik (Glasgow) (Lab): Thank you, convener. I do not believe that I have any interests to declare, other than the ones that I have already declared in my entry in the register of interests.

The Convener: Thank you.

Decision on Taking Business in Private

10:01

The Convener: Item 2 is to ask the committee to agree to take items 6 and 7 in private. Is that agreed?

Members *indicated agreement.*

Green Investment Bank

10:01

The Convener: Item 3 is to take evidence from the Green Investment Bank. I welcome Lord Smith of Kelvin, who is the bank's chairman; Shaun Kingsbury, who is its chief executive; and Rob Cormie, who is its operations director. I thank you for coming along to help the committee with our work and deliberations.

Before we move to questions, does Lord Smith want to say something by way of an introduction?

Lord Smith of Kelvin (Green Investment Bank): Yes, convener—and many thanks for your introduction and your welcome. It is genuinely a great pleasure for us to be here and we very much appreciate the committee's time and interest.

I will take the opportunity to introduce my colleagues and offer an update on progress during what is not yet a full year of operation. Shaun Kingsbury, our chief executive, joined us in November last year. He has held a number of senior global roles in the renewables industry.

Similarly, our director of operations, Rob Cormie, has many years of experience in our sector. He manages our day-to-day operations, including how we manage sustainability, our technical experts, communications, human resources, property and information technology. Most important for today, he is responsible for Scottish project origination.

I became chairman of the GIB in May 2012. I am also chair of Perth's SSE, I am about to depart my role as chair of Glasgow's Weir Group and I am the chair of Glasgow's 2014 Commonwealth games.

To come back to the GIB, one year on I believe that we have made sound progress on the two parts of our mission. The first part is to help to accelerate our transition towards a greener economy. We do that by investing in projects that are both green and profitable, such as offshore wind farms, large-scale waste recycling facilities, waste-to-energy facilities and large-scale energy efficiency programmes. Those are the types of large infrastructure projects that we need if we are to achieve our demanding and legally binding environmental targets.

Our involvement in the projects must be necessary to see them go ahead, so additionality is key, and we must make investments on a commercial basis and crowd in other private sector capital. That is a nuanced role that is in part dictated by state-aid rules that are set by the European Commission, so we have been taking time to explain fully to all our stakeholders the role that we can play.

The second part of our mission is to build an enduring institution. We are here not only to invest the now £3.8 billion of the Government's capital—taxpayers' money—and move on. The challenge that we face in financing our transition to a greener economy demands a type of institution that is here for the long haul, so that is what we are building.

We are, of course, building the new institution with its headquarters here in Edinburgh. Indeed, we are indebted to many of you—Marco Biagi among others—for your support for Edinburgh's successful bid. Last week we moved—with a full complement of staff—into what will be our permanent headquarters in the heart of the city. We now have a total of more than 80 members of the team, with 31 in our Edinburgh headquarters and the remainder in our transaction hub in London. Edinburgh is home to our headquarters functions: risk, finance, legal, sustainability, technical, communications, human resources and operations. It is also home to one of our three investment banking teams—the energy efficiency team.

We have been made very welcome by the wider Edinburgh community, and we have recruited well by bringing in some home-grown talent as well as attracting talent from across the world. I believe that our experience has proved the assertion that was set out in the Edinburgh bid, that this city is already a hub of global financial talent and an attractive destination for talent that is working elsewhere.

Because we are headquartered in Scotland, and as a Scot myself, I have been particularly keen to ensure that Scotland secures at least, if not more than, its fair share of our investment capital. I am afraid that we have not seen that come through yet. So far, we have invested only in a small project at the Tomatin distillery. However, we have a number of positive prospects in the pipeline that we are dedicating ourselves to pulling through.

I am proud of what we are achieving at the Green Investment Bank. The challenge is to build our economy on a low-carbon footing and, as we do that, to capture as many of the benefits for the wider economy as we can. If we do that, we create new sustainable growth. Nowhere is that opportunity greater than in Scotland. We grew up complaining about the weather; now we have a chance to put it to work for us. I believe that GIB is well set up to help to realise this opportunity, and that we can do it by being both green and commercial.

I hope that was a useful introduction. We are now ready for questions.

The Convener: Thank you, Lord Smith.

Members will want to cover a number of issues. We are interested in exploring the pipeline of projects and we might wish to consider borrowing powers, how you are going to support community projects, issues around the Edinburgh headquarters and its footprint here, governance, and issues around risk and borrowing—a wide range of things. We have about an hour, although we might run a little bit longer than that. However, I ask members to keep their questions short, to the point and focused. If we can have answers that are as focused and to the point, that would be helpful, too.

We will start off on the pipeline of projects that you mentioned. Dennis Robertson has the first question.

Dennis Robertson (Aberdeenshire West) (SNP): Good morning, gentlemen. Before we consider the pipeline of projects, I wish to consider something that you said in your introduction, Lord Smith. Thank you very much for that introduction.

You said that you are perhaps slightly disappointed at the lack of investment and you mentioned the Tomatin distillery. I know that the GIB is still quite young, but can you put your finger on why investment has been so poor? Is there a reason why uptake has been slow?

Lord Smith: No—I honestly do not think that there is. I think that that is just how it happens. We have quite a pipeline, however, and you will be hearing a bit of detail on that as we get further into things. There has been no lack of enthusiasm on the part of the Government, local authorities and certain other organisations that are in our space. I do not think that we have a Scottish worry at all.

Dennis Robertson: That is excellent. Could you give us a little bit more detail about what projects are in the pipeline and how confident you are that they will progress?

Shaun Kingsbury (Green Investment Bank): Let me give you a little bit of background about the types of things that we are looking for. When we get into details of projects, Rob Cormie will be best placed to answer, given that that is his main focus.

The challenge in Scotland and across the United Kingdom as a whole is huge, which is perhaps one reason why we have not got off to a very quick start here in Scotland. Across the UK as a whole, we need to invest close to £200 billion in the next 10 years to hit the legally binding targets. If we consider that on an annual basis and divide by 10, that is £20 billion a year that will need to be invested. The run rate that we have at the moment is 25 to 30 per cent of that—£2.5 billion to £3 billion a year, rather than £10 billion a year.

We are looking for projects that fulfil our double bottom line. They have first to be profitable. If you take one thing away from our discussion and my comments this morning, it should be that we are a for-profits bank; we will make a return on taxpayers’ money. Projects also have to be green. Finding projects that are both green and profitable has been the challenge, particularly here in Scotland.

The other area that gives us a challenge is additionality. We are trying to crowd in private sector money—our role is to capitalise private sector investment. If there are projects that already have enough financing—there will be some that really do not need our money—we will not elbow our way into those transactions, because there is no need for us. We want to focus on the green and profitable projects that are a little short of capital. Where maybe 50, 60, 70 or 80 per cent of the capital is available, we will bridge the gap, whether they need debt, equity or some other type of financial support. We want to crowd in the rest of that money, not compete with the private sector to crowd it out.

Rob Cormie will talk a bit about where can invest. We can invest in debt or in equity, in mezzanine or in guarantees, as long as the returns are adequate. Some of the projects that we have seen throughout the UK, not just in Scotland, are green but do not hit our profitability targets. They are not bankable, as it were—they are at too early a stage, the profit margins are not there or the risks do not add up when we look at the potential returns. Rob Cormie can cover the areas that we are focused on and what the pipeline in Scotland looks like.

Rob Cormie (Green Investment Bank): I am delighted to do that. I will do it in two ways. First, whom do we engage with? I want members to understand whom we are talking to. That includes Scottish Enterprise, the renewable energy investment fund, the Scottish green investment portfolio, which was stimulated by the First Minister last year, and the Scottish Futures Trust. All are part of the team that we engage with to try to create opportunities. Some of them focus on slightly smaller areas—for example, REIF tends to focus on smaller community projects and some of the marine areas—while SFT is perhaps more in our sweet spot.

Secondly, I will split into three the sectors in which our mandate allows us to invest. The first is offshore wind. Let us look at who is investing or who may invest, in due course. Through SSE, there is the big Beatrice project and there are projects up on the Moray Firth that are sponsored by Repsol and EDP Renewables. That shows some of the international investment. In the Forth, there is Mainstream Renewable Power, which is an Irish sponsor that has a large base in Scotland. Those offshore projects fit within our mandate and we will seek to work with them over the next year or two. I make it clear, however, that those projects are happening not today but over the next one to three years.

The second sector is energy efficiency. As Robert Smith has said, the i-banking team is based here, so the focus is here. An obvious area that has been mentioned in the press is street lighting. We think that there is a great opportunity for Scotland and elsewhere to reduce emissions through that sort of programme. To the extent that we can be involved, we are delighted to be.

Another area is the estate of Scotland. The national health service is an obvious example—I do not know whether it is the biggest—of a vehicle that is, unlike the NHS in England, under the control of a single unit. We are talking to the NHS about how we might be able to work. The challenge for us is to take 1,000 little projects and put them into a scalable project with which we can really engage. We just do not have the bandwidth to do otherwise. We are also heavily involved with sustainable Glasgow and with some district heating projects.

The third bucket is the waste and biomass area, which I will split in two. There are large waste projects in Edinburgh and the Clyde valley. The Edinburgh one is a bit further forward than the one in the Clyde valley, which is at an earlier stage. We will engage to see whether we can be additional, whether they are green and whether they are profitable. Those projects are very much on our list. On the biomass side, Estover Energy has some small-scale virgin projects in the north, and everyone will be aware of Grangemouth and other projects like it. They fit within our mandate. I will not comment on individual projects, but to the extent that they are in the mandate, there will be extensive due diligence and we will ensure that they are green and profitable.

The pipeline is there and we believe that we are working with the right people. We would obviously like to accelerate it and, indeed, to do more. We would like to get there quicker, but that is because we are impatient folk.

Dennis Robertson: I am hearing a lot about opportunity and potential, but I do not seem to be hearing—correct me if I am wrong—about what is happening now in terms of investment.

10:15

Lord Smith: I will start and then hand over to Shaun Kingsbury.

On the totality, in case you have the impression that we have not done any deals yet other than in Tomatin, let me say that we actually invested £635 million in our first five months. That investment crowded in other capital that took the total value up to £2.3 billion. That includes 11 major transactions, including putting some money into four funds to do smaller deals. Therefore, we have not been idle in the first five months to 31 March.

Dennis Robertson: I was not suggesting that you have been idle, but I am hearing only about potential and opportunities rather than about actual investments that are in the pipeline now.

Lord Smith: We have put quite a lot of cash out already.

Shaun Kingsbury: Rob Cormie has touched on some things, but I should explain that it takes on average three to four years to develop a project, from the idea to securing the land to getting the power purchase agreement and so on. We are aware that, of the £4 billion-worth of transactions across the UK as a whole, only £500 million of those might be in a position to close.

We cannot give details on specific projects that we are close to closing within the next six to 12 months because they are under commercially binding confidentiality agreements. If we were to give our opinion in a public setting that a particular project was great and another project needed some work, we might find that folks would not bring us the information, because they are very concerned about confidentiality.

We have a pipeline of the sort of projects that Rob Cormie talked about, such as for offshore wind and biomass. Those are real projects, about which people have said in the press that they are talking to folks including the Green Investment Bank about securing financing, so we feel comfortable about putting those on the table. However, for a lot of the rest of the stuff, it takes a long time. Where folks have shared stuff with us under a non-disclosure agreement, we would feel nervous about providing any commentary on their projects.

Dennis Robertson: Thank you for that. Convener, I know that other members have questions, so I will leave it there.

The Convener: Before I bring in other colleagues, I want to go back to what Lord Smith said about wanting to ensure that Scotland gets its fair share of projects. What do you think a fair share is?

Lord Smith: A fair share would be more than our population percentage or gross domestic product percentage.

I need to be careful, because the projects need to be green and profitable and have a legitimate organisation. However, I would not want to turn round in two years and say that we have invested only in Tomatin distillery. There is quite a lot in the pipeline in Scotland.

The Convener: I presume that you need, as a UK institution, to be neutral about the different parts of the UK. Even though the bank is headquartered in Scotland, you cannot say that you will prefer Scottish projects.

Lord Smith: Absolutely; we cannot do that.

Dennis Robertson: However, you suggested that Scotland has perhaps more wind projects—and perhaps more in the marine environment, too—that could be taken forward.

Lord Smith: Scotland has 25 per cent of Europe's potential wind energy, 25 per cent of its potential tidal energy and 10 per cent of its potential wave energy, so there should be opportunities there.

The Convener: I will allow a question from Chic Brodie on this issue before we move on to Hanzala Malik.

Chic Brodie (South Scotland) (SNP): Good morning. On that, I have a question on governance. I am concerned that, according to the briefing paper, your Edinburgh office has responsibility for asset management but transaction operations are carried out under the auspices of your London office. How is that circle squared? Can you help us with the actual management of the assets and the criteria for investment?

Shaun Kingsbury: We have two offices, and actually it is great to be in both cities. We have tried to strike the right balance between where we should put people and where the transactions are. Like it or not, a lot of transactions are done in London. That is where the lawyers are, that is where the other banks that co-invest with us are and that is where many of the equity providers are. We wanted to put people in the right place, so that we were not causing them to travel up and down too much between the two offices. If you were working on financing an offshore wind project in Germany, you would probably conduct those negotiations in London, using lawyers based in the City, and you would write the documents in English. For investments such as offshore wind and the waste business, it made sense to put them down in London close to where the transactions and the other investors are.

Energy efficiency is obviously a more distributed kind of business, as there are projects all over the country. There was no need to put that in London, so we put it in Edinburgh. We took all our support—all the folks that report to Rob Cormie—and put them in Edinburgh. We have about 35 people here in Edinburgh and about 50 down in London; that is the split between the two offices.

I am the chief executive of the whole business and Robert Smith is the chairman of the whole business. He sits in Edinburgh, and I spend most of my time in London. On average, I spend two days a week in Edinburgh and three days a week in London.

Chic Brodie: Can I progress this, convener?

The Convener: Seeing as you have stolen the ball from the pipeline, which we were talking about, I will let you carry on.

Chic Brodie: I promise you that I will come back to the pipeline.

Thank you for that explanation, Mr Kingsbury. I am also confused by the private sector involvement. I am not sure whether the private sector is involved project by project and whether you anticipate that, at some stage, the investment bank will issue equity to the private sector.

What role, if any, does the private sector play in decision making? Its involvement is project by project, but what role does it play in deciding the overall strategy of the bank?

Shaun Kingsbury: Our role is to catalyse private sector investment, so we work closely with the sector. For the £635 million that we committed last year, we committed it with one part from the Green Investment Bank and 2.8 parts from everyone else—about a 1:3 ratio. We provided just over 25 per cent of the capital. We do that project by project at the moment, as Chic Brodie suggested in the question.

A project developer or utility will bring us a project and tell us that it has solid debt organised and needs appreciative equity, or that it has all the equity organised and is short, for example, £50 million on the debt syndicate. We then fit in. We take the same price as the other investors, so we do not generally set the price. We fit in with the terms that they provide.

Going forward, instead of crowding in that money transaction by transaction and project by project, we will think about going out and finding institutional investors—people with long-dated capital that meets the long-dated nature of our assets, which are typically 20 years in operation. We will tell them that we have a portfolio of opportunities and a £4 billion pipeline of opportunities that could close off in the next two or three years and ask them whether they would like to give us some money up front. That would enable us to crowd the capital in first and then immediately go and work with those projects because we would have the private sector capital sitting beside us.

We cannot do more than 50 per cent of any transaction, whether on the debt or equity side. We have been successful in doing 25 per cent on average, during our history.

It is clear how we work with the private sector, but we will consider ways of crowding in the capital first rather than transaction by transaction, which is what we have done to date.

Chic Brodie: Capital is not flowing as quickly as we would like, but there is clearly competition for cheap capital. Under the auspices of Scottish Enterprise, we have the Scottish Investment Bank, which has a renewable energy investment fund to promote use of energy from renewable sources, so there are two bodies that are under Government auspices competing. How do you relate to the Scottish Investment Bank?

Rob Cormie: We are complementary to the SIB to all extents. I am sure that you are aware of where the Scottish Investment Bank's capital came from. It has a specific mandate to consider local community projects of a slightly smaller scale. It has also spent more time on earlier-stage wet renewables—marine and tidal. There is a little bit of overlap there because that sits in one of our sectors, but the Scottish Investment Bank has tended to consider much smaller deals that are at an earlier stage in the capital cycle.

The Scottish Investment Bank takes a slightly higher-risk position than we do in our investments, for which the need to make a commercial return is one of the key drivers, alongside the green element. We see it as a complementary source of capital. We often receive inbound calls that we redirect either to the REIF, the Scottish green investment portfolio, the Scottish Futures Trust or wherever we think might be the most appropriate pool of capital.

To be frank, it is important that we work as a team. The Green Investment Bank is not the panacea; it is one intervention. The REIF fulfils a complementary role alongside us.

Chic Brodie: I have one question that comes back to the pipeline.

The Convener: Before that, does Marco Biagi want to comment on governance?

Marco Biagi (Edinburgh Central) (SNP): I do not want to disrupt the smooth running order.

The Convener: That has already gone way, way out of the window.

Marco Biagi: I will run with the ball for quite a few questions on governance, convener, if I may.

The Convener: Given that governance has been raised, we will deal with that and then go back to the pipeline.

Marco Biagi: I will go back to what was trailed at the start about the governance split between Edinburgh and London. Lord Smith said that 35 people are employed in Edinburgh and about 50 in London. I am a layman, and that does not strike me as being what the average person on the street would think of as an organisation being headquartered in Edinburgh with a branch in London. It looks a little bit like the opposite. What are the 50 people in London doing? We had the breakdown of jobs in Edinburgh, which include risk, finance, legal, sustainability and operations jobs.

Lord Smith: The people in London are deal-doing. Apart from the energy efficiency team that is based in Edinburgh, which is a deal-doing team, the deal-doing teams are all based down in London. Incidentally, all board meetings—except very occasionally when we cannot get people together—take place in Edinburgh, and there are four Scottish directors out of nine on the board down there in the GIB. However, when it comes to what those guys are doing down there, I would like to know.

Shaun Kingsbury: Would you? Okay—I will see whether I can inform you better. What they do is focused on the transaction side. We have two or three parts to that. We have a strategy team that works on where we should be investing and what is happening in the market, so that we understand that. We also have capital markets folk—we supported the Department for Business, Innovation and Skills in the initial public offering of a very important transaction that took listed project equity to the main market in London. What we do with the capital markets is based in London because the market is in London.

The investment teams in offshore wind, waste and biomass are in London; each has about 10 folk plus a couple of support folk in them. That is basically it, in London: capital markets, strategy and each of the transaction teams. Such deals are done in London, as I said. If you were financing a German wind project and you had a Swedish investor, you would probably end up coming to London and producing the documents in English. That is the market.

We are very conscious of our green footprint, so we use videoconferencing a lot between the two offices. We did not want a pile of people sitting in Edinburgh who would, first thing on a Monday, get the train or fly down to London, spend the week living in a hotel and then get the train or fly back up on Friday night.

Marco Biagi: I appreciate that that is not a very desirable situation. It would certainly not be a very green situation.

Shaun Kingsbury: Exactly.

Marco Biagi: You referred to deals being done in English with lawyers in the City. We speak English in Scotland as well and we have quite a lot of lawyers in Edinburgh. The situation strikes me as being a little bit London-centric and—based on your description—I think that an observer would not be faulted for saying that the meat and drink of what you do happens in London and you have a back-office function in Edinburgh, plus your board meetings.

Lord Smith: I take issue with that, somewhat. Our energy efficiency team, our experts—technical experts as well as deal-doers, financiers and so on—are absolutely based up here. Sometimes they have to go to Manchester or Birmingham on missionary expeditions and so on. However, do not make any mistake: even for the Royal Bank of Scotland, its core teams in things such as project finance and its green teams are based in London. Very few of them are here, although the bank is headquartered up here in Edinburgh. To meet like-minded people, you have to be down there.

There is also history to GIB. It was housed initially in London—there were front-runners, if you like, way back about 18 months ago. A team was gradually being built up to work out green policies and things like that, and it was based in London because no one knew where headquarters were going to be at that stage, so there is a little bit of a legacy. However, a lot of the very senior people are based up here and I would not just dismiss Edinburgh as a back office. The whole legal headquarters and IT and HR and so on are based up here.

Marco Biagi: What is the difference in salary spend? Do you have those figures?

Lord Smith: Do you mean between London and here?

Marco Biagi: Yes. How much is spent in Edinburgh and how much is spent in London?

Shaun Kingsbury: The average salary across the bank is about £110,000 per annum. It is about £80,000 in Edinburgh and it is about £120,000 in London, so London people cost more.

Lord Smith: So, the maths is sort of 30-odd times £80,000 plus 50 times £120,000.

The Convener: Okay. Hanzala Malik has a question that takes us back to pipeline issues.

10:30

Hanzala Malik: Lord Smith will be aware that Glasgow is the centre of the universe, so I will initially stick to talking about it.

I came across a newly established company called Greens Waste, which is very keen to create energy from recycling. My heart of hearts tells me that it is not aware of your operations or your facilities. Given that it is a small company in its infancy, would you consider mentoring and bringing the company on board so that it could benefit from what you do? You, too, would benefit from that company's profit margins.

Lord Smith: First, given that the Green Investment Bank has a £3.8 billion turnaround and a staff of 80 people, it cannot go chasing deals of £500,000, £1 million or £2 million. We tend to invest about £30 million from our main fund; that is our minimum take in any one transaction. However, we have delegated money. We have invested in four different funds—my colleagues will go into the details—for companies that do different things, such as waste or whatever. If your people want to speak to those dealing with one of those funds, we would be delighted to introduce them, because they deal with companies at an earlier stage of development and do much smaller transactions than we do.

Shaun Kingsbury: Let me tell the committee about the rationale behind that. As Lord Smith said, we need to focus on the larger transactions. However, we fully recognise that there is a group of younger, smaller companies throughout Scotland and the rest of the UK that do not need £30 million or £40 million because they are not at that stage of development. What they need is £5 million for the first pilot-scale plant. The economics would work and that would meet our green criteria.

We ran a competition to find two fund managers. We gave them a tight mandate and they came and pitched us on their background, their knowledge of the market, the deal pipeline they had, the networks in which they could find things and their experience of making such transactions work. On average, we gave about £50 million to the four successful projects, with one getting £30 million. Two were funded to carry out waste-to-energy and biomass projects and two were for energy efficiency projects, which are, typically, smaller projects.

The first round of investment has been made. In fact, the project that we backed in Scotland was through one of those funds. That was a relatively small investment of just over £1 million. It was not an investment that the Green Investment Bank probably could have done, but it shows that that mandate is working.

Where there are earlier-stage or smaller but bankable, green and profitable projects, bring them to us and we will direct them to the right folk and they can see whether that works for them.

We are not in the job of mentoring; it is just not possible for us to mentor all the companies. We act purely like a bank. If someone brings us a good project that is not quite yet bankable or ready for significant capital, we will certainly lay out what is needed, such as the need for purchase and supply agreements to match the tenor of the loans, and things like that. With just over 80 staff, we do not have the capacity to send folk out to help others to set up or explain their business. We will tell them what is missing and ask them to bring the project back when it is ready.

Hanzala Malik: I got the feeling—it may be misplaced—from your presentation that you are almost cherry picking and going only to councils and big, established organisations, thereby denying the Johnnys-come-lately. A lot of those companies are fresh thinking and you are missing out on that. You are not really there for the small guy, who is important. Are you going for the easy kills—the councils and local government—or are you going out to industry? How are your investments split?

Shaun Kingsbury: We are doing that—we are not just investing in well-established companies. This year, post our financial results, we announced a transaction for a combined heat and power biomass project in Northern Ireland. That £80 million project, which is being developed by two brothers, is large for a first project. It is therefore possible for folk with projects to come forward. Of course, they had lots of support and advice, they had backing from export credit agencies and the utility in Northern Ireland signed a power purchase agreement with them. That is not small scale, but it was a first time.

On smaller-scale plants, we are here to back a very large-scale transition to a greener economy. The large-scale projects that we consider—for example, offshore wind farms—can typically be between £500 million and more than £1 billion. Those types of transactions are very short of large-scale capital. We are just not set up to go from providing £50,000 loans to providing £200 million loans—it is not possible to cover all those things at the same time. However, we have thought about it and have set up funds to deal with people with new projects and people who need £2 million, £3 million or £4 million. Those funds are investing money.

The £1 million investment in Scotland, of which £585,000 came from the GIB through the fund, is a relatively small investment. However, the interesting thing about it is that it is the first and we believe that we will be able to use it as a kind of cookie cutter. A large number of places could take the same biomass boiler. Having done the first one, which is always the most difficult, we can replicate it again and again with the same providers, the same technology and the same financing.

The Convener: I ask Margaret McDougall whether her question is on the pipeline issue.

Margaret McDougall (West Scotland) (Lab): No, it is on investment.

The Convener: Okay, I will come back to you in a minute. Chic Brodie has a question on the pipeline.

Chic Brodie: I have two brief questions. First, given that, as I read recently, down south, at peak load, the Government faces a 4 per cent safety margin and therefore there is a lot of pressure in the system, I ask Lord Smith whether he is facing any political interference with projects that might be done more quickly. My second question is for Mr Cormie, who mentioned district heating systems. Have you had any conversations with Scottish Coal interests, given the opportunities that there are to use the resource that is now lying in disused coal mines to provide district heating systems in communities in Scotland?

Lord Smith: On the first question, I can tell you that there has been no political interference, slightly to my surprise.

Chic Brodie: It is coming.

Lord Smith: I expected that Vince Cable's constituency might be the preferred route for some of the money, but I promise that there has been no political interference. Sometimes, when you are putting deals together, you suspect that there might be something going on behind the scenes but, honestly, there has not been any interference.

Shaun Kingsbury: There has been tremendous support from everyone.

Lord Smith: For the avoidance of doubt, that includes north of the border.

Rob Cormie: On Scottish Coal, I am not aware that we have had conversations on that, but I will double check and get back to you with an answer. I am not aware of any such conversations, but it is a good idea.

Marco Biagi: On the pipeline, you referred to your position with regard to affordability and a return. How does that fit with the necessity to invest in projects that are inherently risky? Where is the GIB's additionality above what a company in the pipeline might be able to get from a fully commercial investor, which will be looking for profitability, too?

Shaun Kingsbury: I will have a go at answering that, using offshore wind projects as an example, as we can all easily get our heads round that. People come to us and say that they would like us to invest in their offshore wind project. They say that they can afford so much equity, that the banks have provided so much debt and that they need us to fill up the difference. They offer to pay us a flat rate of return and we will take the first loss. They might also be a bit worried about their short-term debt, so they ask us to underwrite the refinancing risk that might come in three or four years when they need to do that. By the way, they might be a bit worried about how the contracts for difference or renewables obligation certificate regimes will work, so they ask us to guarantee some sort of floor on the power price because, if we do that, they will be able to mobilise all the capital that they want and they will get 10 of the things built.

We politely say no to most of those requests. The reason for that is that we are trying to create a market that is self-financing over time, and we cannot do that just by taking away all the inherent risks in the projects from the project developers and taking them on to our balance sheet, because we have only £3.8 billion. As I outlined at the beginning, the size of the low-carbon-generation need is £110 billion. If I took on those risks, I would use all of that money and, invariably, a load of them would come home to roost. We would burn through our £3.8 billion; we would have a whole load of losses; the Green Investment Bank would cease to exist; and the problem would still exist in the market.

We need with the market to find solutions to and fix problems such as who should own the power price risk, the construction risk and the refinancing risk and allocate those risks and, in turn, the returns that come with them in a way that allows capital to flow and allows us to use our money judiciously. As a result, that money will go further and we will not see losses.

How do we square that with additionality? It is all about the sheer scale of what needs to be done. Given that we would back only green and profitable projects, if, say, only £5 billion of investment were needed, there might be enough money in the banking market to fund that; in that case, given that we would back only green and profitable projects, you would not need us. However, £110 billion is going to be needed over the next 10 years, and the fact is that there are just not enough banks or capital.

We invest on the same terms. In the case of refinancing, say, offshore wind projects, we sit in the banking syndicate and get all the same terms that other banks get. However, whether we are buying or refinancing, we get a commitment from the lead arranger of that capital that they have gone out and looked all around the market to raise £250 million; they might have raised £185 million or £200 million and really need us to come in. We will take the same terms as the rest of the banking syndicate. We do our own due diligence, reflect on the return and ensure that it is adequate to cover the risks and that it represents the market so that we are not in any way undermining it. However, we do not set the price, which is why additionality really counts.

Lord Smith: This is quite a tricky issue. After all, how can you be profitable and at the same time promote additionality? Because the banking market is not yet perfect again, one issue is the length of lending and the refinancing risk. Another issue is that banks are quite jittery. You might have a syndicate of five banks ready to do something; one of them might fall out and we can come in and plug that gap. That is a commercial activity because we are saying, "These other commercial people would have done it at these rates," but the fact is that without our taking such action the syndicate would not happen.

Indeed, I can tell the committee about one particular transaction that is a classic example of our filling a gap in a syndicate. Right now, we are speaking to a Japanese organisation that is not a bank but is a supplier of something offshore. Unless we had been investing alongside it, it would be too nervous. We are not saying that we can provide any guarantees about the renewables obligation certificate regime, contracts for difference or whatever is going to be in place, but we give a Japanese level of comfort that a Government-backed bank is present.

Finally, I would like Shaun Kingsbury to explain one example—the Greencoat deal—in which we broke the mould and something happened that would never have happened without us.

Shaun Kingsbury: We want to bring in the right type of capital, because these projects involve 20-year capital and need long-dated finance on the debt and equity side. Institutional capital is the capital that sits in all our pension funds and investments to look after us in our retirement. Pension funds allocate perhaps 50 or 60 per cent of that to very safe things such as Government bonds; they might then put 30 per cent into equities—in effect the stock market—and 10 per cent into a variety of things that they call alternatives. A small portion of that will go into infrastructure and a small portion of that will go into renewable energy infrastructure.

Because it is very difficult to battle for only a couple of per cent of the whole pie, we wanted to target the 30 or so per cent that pension funds hold in equities. Today, if you want to invest in renewable energy infrastructure, you have to go through a private fund mechanism and we wanted to bring to the main market in London a vehicle that would target that bigger 30 per cent pool of capital in listed equities. Two years ago, a team assembled a group of assets that they tried to list to raise £200 million on the alternative investment market; however, they were unable to reach that total. We restructured the list, brought it onshore, took it to the main market and committed £50 million to it. The list is managed by us but held by BIS, and the team succeeded in acquiring and listing the assets. This time, when they went to list, they had to raise between £205 million and £260 million, and the offer was significantly oversubscribed. In fact, globally, it was the biggest IPO in the renewable energy business in the first half of the year.

10:45

Since we concluded that deal, four or five additional companies have come to market with very similar offers, many of which have succeeded in listing. We demonstrated that that could be done, and we got the first one away. We did not think that it was risky capital, and that is why we were willing to do it, but it was risky in the sense that it put our reputation at stake, and it was risky in the sense of being novel and innovative. As a result, there are now four or five funds, and there are hundreds of millions of pounds from that 30 per cent pool of capital now coming into the market, which was previously precluded because there was no vehicle in which to invest. That is the type of stuff that we are trying to focus on: innovative, green and profitable.

Marco Biagi: Where does that leave the technologies that were described as wet renewables before—the fledgling technologies such as offshore wind, wave and tidal? I am thinking of wave and tidal in particular. Are they left to go to other sources such as REIF, which you mentioned?

Rob Cormie: Although wet renewables sit within our remit, we always go back to the need for projects to be green and profitable. There is no doubt about the green part, and you could argue that they would meet the case. On the economics, having worked with some of the companies from the past, I think that they are going down the traditional route of seed capital and the friends and family route for the initial invention, but they are now sitting in the hands of the people who are best able to nurture them, which are Siemens, Alstom and ABB—the very large engineering companies—which will now take them from fledgling businesses with a great idea and a potential market to ones with commercial rigour and proven technology.

We see the sector as more of a watching brief for us. We would like to engage, which is not a problem—we want to be part of the debate—but we view that sector as a watching brief for us and one that is for others to invest in. As and when we can invest alongside other commercial institutions, we will no doubt be considering that. However, that is something for the future.

Shaun Kingsbury: It is incredibly important to demonstrate the green and the profitable in our early transactions. Thinking about the comments that Robert Smith made at the beginning of the meeting about creating "an enduring institution", I note that, for a bank, that means the ability to raise capital, and we will be able to raise capital only if our projects are profitable. So far, all our projects look good. They are very much at the less risky end of the spectrum, ranging from venture capital through private equity to infrastructure, and they are definitely more on the infrastructure and senior debt side.

By building a track record over time, the bank will be able to access more and more types of private capital. If we were to take on those early venture capital projects, which are inherently risky and much more likely to lose money, there might be some winners and some losers—that is what a venture portfolio typically looks like. The losers that we would have as a result are disproportionately difficult for us in these first few fledgling years of the bank. As we go out to raise the capital to build an enduring institution, we need to do so on the back of profitability, and people will be looking carefully at the first few years of operations and the investments that we have made.

We are definitely on the infrastructure, and we will do debt or equity or guarantees. That is much less risky. We need others to step up and do the venture capital piece that moves projects down through the cost curve and up through the reliability channels. When those represent an infrastructure-like investment, we will be right there, ready to do it.

Marco Biagi: Could you envisage moving into that venture capital role later, as you become established and when you have built the capital?

Lord Smith: Some of us come from a venture capital background, and we would love to be in there.

Marco Biagi: I will take that as a yes.

Shaun Kingsbury: We are restricted, however.

Lord Smith: If we start spraying small amounts of money around and half of the projects concerned go bust, we will be closed down.

Marco Biagi: Lastly—[*Laughter*.]—I am playing the Mike MacKenzie role—do you think that there could be more confidence in the sector, in particular from commercial investors, if there was, for example, a headline decarbonisation target at UK level, as we have in Scotland for energy supply?

Shaun Kingsbury: We are in the middle of a process called the energy market review, as I am sure you know, led by the Department of Energy and Climate Change down in Westminster. The Energy Bill is a hugely important piece of legislation, which represents probably the biggest change in the energy market since the break-up of the Central Electricity Generating Board. It aims to provide more comfort to investors. They are more likely to be investors with more of a financial background—infrastructure investors, who are the type of folks we are trying to crowd in as we do the deals. It is designed to take away a lot of the risk. If someone invests in a renewable energy project today, they get 1 ROC, 2 ROCs or 0.9 ROCs, and the rest of their price floats with the power price.

Those investors are investing in a 20-year asset, but they do not know what the power price will be in four, five or 10 years, so there is a significant amount of risk, which is causing the cost of capital to go up and the availability of capital to go down, so we must provide a bridge to the £110 billion of investment that I mentioned. When electricity market reform gets rolled out, you will get a contract for difference, which is in effect a fixed price for 15 years. For the first time, if people are sinking their capital into an offshore wind farm or a waste-to-energy plant, they will be able to say, "I know what I will get for each megawatt hour of power that I produce for the next 15 years. I can go out and get very safe long-dated capital, which has a lower cost, and that will bring the total cost down." That will be great for the UK and we need to see it happen.

Anything that helps to signal the commitment to the long term, which is what your question was about, is very helpful to us, because as people—many of them are foreign direct investors or foreign engineering companies—start to come to the United Kingdom and commit to look at the projects, commit to work with us and the commercial banks and commit to having a significant presence, any signals are definitely helpful.

When you make as significant a change as this, the process always has the unintended consequence of slowing everything down, because everybody waits and asks, "Should I do this project under the existing regime or under the new regime? What capital structures would work?" There is therefore a hiatus in investment levels, as we would reasonably expect. The sooner that DECC—we are supporting it and helping it—can work through the details and get them out, which it promised to do before the end of the year, the sooner we can again make progress on investment levels.

The Convener: Mark McDonald has a question on risk and four members are still waiting to come in. I am conscious of time, given that the evidence session has now lasted for 50 minutes, so we need to sharpen up our questions and answers a bit, please.

Mark McDonald: I have a couple of questions, but I will start with one on the balance of risk. I am not sure that I have seen that balance coming forward yet.

Obviously, after the banking crash there was a move to extreme risk aversion in the lending sector, in which there had previously been a gung-ho attitude in many respects. Where do you sit between those two extremes? If all that you are doing is offering the same risk-averse approach that the banking sector currently offers, what are you bringing to the table for these projects that they cannot already get in the financial markets?

Shaun Kingsbury: As I alluded to when I answered previous questions, if you think about investing in renewable energy as a spectrum from venture capital through private equity investment, development investments and building infrastructure, we are definitely at the less risky end of the spectrum. We are not doing venture capital and we are not taking development risk.

One reason why what we do is additional is that there is the big gap that I pointed out—the £110 billion of low-carbon assets that we need to build—and there is not enough capital to do those projects now, so what we do is additional. Another reason is that many of the new potential sources of capital are foreign direct investors and financial investors and they take a lot of comfort in being able to invest alongside a company—a bank—that is owned by the Government. They feel comfortable about the regulatory regime and if they are in the same piece of the capital structure with the same returns and the same risks, they feel more comfortable about that.

Mark McDonald: Obviously, one person's risk is another person's opportunity, so that balance must also be struck.

Profitability obviously plays a major role in your decision making. Is there a specific point at which you would expect the investment to start turning a profit? Given that many projects will not be instantly profitable, do you specify a time by which you must turn a profit or investment will not be forthcoming?

Shaun Kingsbury: Because it is infrastructure, we do one of two things. Either we invest in the operating plant in return for the utility—usually—that owns it reinvesting the money in building the new plant, or we invest in construction. Everything is lined up; it is not like making a private equity investment in a company that needs to grow market share and build things.

When we make our investment in, for example, a waste-to-energy plant, it needs to have a 20-year waste supply contract if it is a large plant or, if it is a smaller one, perhaps a 10-year contract. It also needs to have a power purchase agreement, a fixed-price contract to build the plant and a fixed-price operating contract from a known and reputable operator. We lock all those things in. In order to be at the lower risk end of the spectrum, we take away all those risks through a lot of contractual negotiations.

Therefore, the projects are either immediately profitable, because we buy into an operating plant and the owner reinvests, or they will become profitable upon the completion of construction and when commercial operations start. So far, all of the projects are in line and we have had no problems with any of our investments.

Mark McDonald: To be clear, some projects will not be able to get in place some of the things that you are talking about without having the finance behind them. Are you not in a chicken and egg scenario in which you ask for projects to have long-term contracts in place, but they cannot secure such contracts without the security of finance behind them?

Shaun Kingsbury: It is an iterative process. When we have done a bit of work, we sit down and give the people behind the project an expression of interest letter, which they then take off and try to get the contracts. They then bring those back and we turn that into a memorandum of understanding, which they take back. That is why it takes three to four years from the idea—for example, that someone would like to build a biomass CHP plant beside a harbour—to the project being lined up. All those things have to come together in the end, and the finance is only one part of a complicated process. That is why it takes so long.

Mark McDonald: I have a final, brief question, which is on the balance between investment in new infrastructure and new projects versus investment in existing or long-standing projects. Are you considering allowing district heating to expand, for example?

Shaun Kingsbury: We would love to find new projects and more ways to extend existing district heating systems. Energy efficiency is a great area, as it needs little Government support, as it stands on its own two feet, and it is incredibly green. I ask everybody, if you are aware of opportunities to extend district heating or put in new district heating schemes, to please bring them to the bank, as those are exactly the type of projects that we would love to back, but we struggle to find ones of sufficient size and quality.

Alison Johnstone (Lothian) (Green): From listening to the evidence this morning, I have the impression that you might be more aptly entitled the big green projects investment bank, although please correct me if that is wrong. We are in community energy fortnight, and I am interested in what you see as your role—if you feel that you have a role—in investing in community renewables. Mr Cormie mentioned that you could perhaps support 1,000 little projects if they were rolled into a bigger project, although Lord Smith suggested that you are concerned about spraying small amounts of money around and the risks inherent in that. Are smaller projects always more risky? Is it possible to amalgamate lots of smaller projects? I am a bit concerned that smaller projects will look at the Green Investment Bank and think, “That’s not for us.” The bank is based in Edinburgh, but it might not be able to help the local authority in the area if it wanted to set up its own energy company.

Shaun Kingsbury: I am afraid that small-scale renewables, such as community wind, solar or energy efficiency projects, are some of the things that the folks in Brussels have said that there is plenty of capital for, so they are not allowing us to invest in them. On the areas that we can invest in, 80 per cent of our capital is in offshore wind, waste to energy, waste recycling and non-domestic energy efficiency, which means bigger projects such as waste heat recovery projects. We can put 20 per cent into carbon capture and storage and wave, tidal or bioenergy projects. Unless small projects are purely on energy efficiency, however, we are not allowed to participate, because the view is that there is enough capital for them.

If we could find someone who had the ability to roll up projects so that they were not a bunch of small projects but an amalgamation, and if there was a way to put all that together and refinance it, that would be exactly the type of thing that we would love to do. We would love to do more on that, but smaller projects typically have less well established developers, less corporate governance and are harder to manage.

To return to your question, we are the big Green Investment Bank. The focus is to make a dent in the required £110 billion, and we need to do that £50 million or £100 million at a time. If someone can put together smaller projects into £50 million or £100 million projects, we would love to do them.

11:00

Alison Johnstone: The UK Government has stated that you will have borrowing powers only from 2015, when the target for debt has fallen as a percentage of GDP. However, the Office for Budget Responsibility estimates that the peak of public sector net debt as a percentage of GDP is likely to occur beyond that, in 2016-17. You are waiting at the moment. What do you bring to the table that is over and above what other funding streams are providing? Apart from skills in investing money and so on, can someone come to the Green Investment Bank and get additional information that will make them think, “Yes, this is the place for me to go”?

Shaun Kingsbury: I will deal with the borrowing part and then come back to the subject of information and advice. When the spending review was announced and there was another £800 million of allocation, that came with an ability for the bank to borrow from the Government in 2015-16. That gives us additional borrowing powers.

As for what I am focused on in our first few months, we have had a great start in moving forward with £2.5 billion of projects, and we are committing more than £700 million of our own money to those. If we are successful in building a successful institution that is both green and profitable, there will be a variety of sources of capital available to us—I mentioned private sector capital when I was answering an earlier question.

I am really focused. With £3.8 billion, we have more than enough capital for the next couple of years. Let us build a successful institution. Let us build something that can access different types of capital, based on profitability. That is not a barrier for us at the moment.

We provide specific advice on what it takes to make a project bankable. We see lots of projects and, of the £4 billion in our pipeline, we have probably seen twice the number of projects. The £4 billion covers ones that we think are on a path to success and that we can back over the next couple of years. When people have come and told us about their plans for all those projects—and for some that did not make the cut—we have made things clear. It is like what I said in answer to the previous question: they will need a power purchase agreement, a waste supply contract and a fixed-price contract to build the plant, and there are four or five guys who typically do that work. They will need to get someone who can do the operations. We will describe to them—we will send them a letter if they ask for it in writing—what it would take to turn what is a really good idea into a bankable project. We provide that type of advice. We do not have an advisory person in the bank, who makes money from advising people, but we tell people what it will take to take their early-stage great idea for a project to something that will stack up and will be investable.

Margaret McDougall: I feel that I have been waiting a long time to ask this question. In some of your previous answers you have spoken around the answer that I am looking for. The projects obviously all depend on capital investment—or most of them do. If we are discussing investment, that means banks. Lord Smith mentioned earlier that banks are a bit jittery just now. Is that because of the uncertainty around the markets in general, or is it more to do with renewables and the changes to subsidy for renewables?

Lord Smith: There are two answers to that. First, there is uncertainty about the change from ROCs to contracts for difference. The Government has to be very careful. It has to be generous enough and certain enough about such things to encourage the market. You have seen the debate about nuclear power and so on. If we go too far down that line, the British consumer could be paying for a very long time for a very expensive form of electricity.

On the other part of your question—I am sorry—

Margaret McDougall: It is the general point about the situation of banks.

Lord Smith: The problem is really at the longer end. Under Basel III—or Bâle III, depending how you pronounce it—the idea is for banks to borrow short, lend short, to borrow medium, lend medium, to borrow long, lend long, and to borrow equity and take equity risk. If a bank lends over a period of 10 or 15 years, it has to have such a capital buffer that it will say, "Crikey, this is becoming less economic."

On the one hand, we are trying to ensure that banks do not get into the position that they were in before by having very large capital bases but, the longer they lend, the more capital they will have to keep. That curve is really quite steep, and that requirement deters banks. Do we want them lending 20-year money and borrowing on the market overnight? No, we do not, but that is what is slowing things down.

Shaun Kingsbury: I will give you an example. We have started to become involved in a number of waste private finance initiative/public-private partnership projects. The projects take four or five years to secure the waste supply contract, find the location to build the site, get planning permission and get the construction done—all of that stuff. Typically when they make the bid, they go in with a banking consortium that is willing to finance it. Typically they get 25-year waste supply contracts—the plant is designed to operate and be around for 25 years—and they need 15 to 20-year debt to support the equity to get the returns to make the pitch.

Having won the processes, some of the waste companies are finding that their finance providers—the banks—are coming back to them and saying, "We're very sorry—this went through a credit committee two years ago and we were able at that point to provide 15-year capital, but we are only able to provide seven-year capital now. That is the maximum the bank can do, so we're afraid we're going to have to step away from this."

Those projects are ready to go so we have stepped in and taken the bank position, providing the project with 15-year capital. Some Japanese banks and some banks in mainland Europe still feel that they can provide that capital but a lot of the banks in the UK are switching from 12 to 15-

year debt to seven-year debt. However, long-dated projects need long-dated debt, so that is a challenge.

Margaret McDougall: Given that you are a Government-funded bank, do you have any influence in the banking industry to help with that situation? Also, when are we likely to have answers on the renewables situation and the change from ROCs?

Lord Smith: The Department of Energy and Climate Change says that it will have answers on the renewables situation by Christmas. It already has proposals out and it is seeking consultation. It reckons that it will nail that down by Christmas this year, so that is one of your questions answered.

Margaret McDougall: Will that appease the banks? Will they then feel more comfortable about lending?

Lord Smith: The banks will feel more comfortable about that part of the equation. They still have the strictures coming out of Switzerland, from Basel, about having to keep very large capital sums and a lot of the banks are still working their way back into profitability. There is uncertainty around that. Also, the banks do not want to go back to reckless lending again. The supply of money to small and medium-sized enterprises is tricky because again, as we mentioned earlier, that money could go out and they could lose some of it. We have all been in the venture capital industry in the past and we know that you get a big winner and some losers.

Shaun Kingsbury: On the other question about whether we can influence the banking market—

Lord Smith: I avoided that one.

Shaun Kingsbury: Yes—thank you. I do not think that we can influence the larger banking market. That is very difficult for an institution such as ours. However, we can influence people around specific projects. They will feel more comfortable when they are investing alongside not just any institution but a UK-owned institution that has Government money sitting beside it. That gives comfort to foreign banks outside the UK in particular as regards our regulatory regime and the fact that they are sitting in the same place in the capital structure as a Government-owned bank. We can be influential in that area and we have seen that in a number of investments that we have made.

Margaret McDougall: Okay. Thank you.

Mike MacKenzie (Highlands and Islands) (SNP): I have been listening to all this with great interest. It strikes me, though, that fundamentally there is an issue. You talked about a £200 billion investment being required over the next 10 years or so. Some commentators are suggesting that much more than that is needed. Given your initial capitalisation and the parameters in which you have to work, do you not think that really, you are just not big enough to make the required difference?

Shaun Kingsbury: In the words of Kermit the Frog, "It's not easy being green." [*Laughter*.] We have a big job to do—we really do. We can only be successful at crowding in the rest of that money if we turn a profit on our initial £3.8 billion of capital. My role is to ensure that we are a successful organisation. If we are a successful organisation and we can show that investing in debt or equity in those projects is profitable, other people will come and join us—that is where the money will come from.

Mike MacKenzie: I can see that. The bank needs to grow quite significantly in order to make the required difference, but I do not see how you square that with the very tight operating parameters. Obviously, you need early success and in order to get that, you are perhaps risk averse, but I do not see how you square the particular circle or deal with the two lines on the graph of aversion to risk and the growth that you require as a bank to make the difference that needs to be made to get to where we need to be with the minimum of £200 billion investment.

Lord Smith: It does not feel that we are short of capital right now, because the deals are not around. You have just heard that, because of the pricing uncertainty and so on, many deals are just not happening, so we have plenty of capital to see us through. However, I think that things will evolve if we develop the bank.

I would like to indulge in a wee bit of history. In the 1960s, I was privileged to join the Industrial and Commercial Finance Corporation. That was just after the war. British industry needed to be rekindled and the banks were flat out. They could not really provide long-term capital and equity capital, and the ICFC was set up. The Government twisted a lot of arms and the Bank of England put in money. The ICFC was quasi-Government, but it had a social purpose. It was there to help small and medium-sized companies with long-term capital and equity capital, for example, and we made thousands of investments. It was so successful that imitators came out of the woodwork. NatWest decided to set up an equity thing, Barclays decided to set up an equity thing and long-term loans for small and medium-sized companies, and before we knew it, a whole market had developed. We developed huge skills, and people left the ICFC and founded venture capital organisations of their own. Eventually, we will no doubt end up with equity partners who are not the Government, with the Government still being sure that we will stick to our green credentials. If we could create that kind of market, which will take a few years—it cannot be done in six months or a year—we will have succeeded mightily. Funnily enough, with the ICFC, people did not work themselves out of jobs. It remained a very large organisation, but it spawned all sorts of imitators and a whole market. That is the dream, as far as I am concerned.

Mike MacKenzie: You talked about the investment hiatus in the whole industry. That is absolutely correct, but do you not think that, when the UK Government sets the contract for difference strike prices and gets that right, there will almost be no need for our Green Investment Bank and that, if it gets it wrong, you will not have sufficient resources to make the difference?

Lord Smith: What a pessimist you are.

The Convener: We are used to it.

Mike MacKenzie: Actually, I am an optimist, but if I do not ask you such questions—

Lord Smith: If the Government gets it about right—it will not get it perfect—I think that it will unlock. From having other hats on, I know that there are a lot of schemes out there and that fields such as Beatrice and Galloper just off the Thames could be accelerated quite quickly if there was some sort of certainty over the next 15 to 20 years. Everyone is waiting for that to happen, and there could be a surge. If there is a surge, people will still need capital. We will then say, “Hey, we might run out of our £3.8 billion. Maybe we’ve got to go for more.” If the Government does not provide that, someone else will. If we are successful, we will attract both debt and equity capital. If the Government gets it totally wrong, some things will not be built. If it gets it wrong the other way and the scheme is too attractive, the British taxpayer and consumer will pay dearly for it. It is a very difficult line to row.

Mike MacKenzie: I am just exploring the possibilities, but—

The Convener: I am conscious of the time, Mike. Would you come to a question?

Mike MacKenzie: Yes. Surely you would get more bang for your buck investing in the risky areas—the new technologies that nobody else is prepared to touch. There is a part b to the question. I wonder whether you are interested in investing in interconnectors? It seems to me that that is low risk, but there is a problem, in that although the island groups have huge energy-generating potential, the Office of Gas and Electricity Markets’ rules mean that a disproportionate share of the cost of the interconnectors must be borne by the first big project involved. That has locked out the energy because no project has emerged that is big enough to pay for interconnectors. It seems to me that there is a low-risk opportunity to achieve a very big bang for your buck.

11:15

Shaun Kingsbury: We use a two-by-two matrix to balance risk and green impact. We try to do the things that have the lowest risk and the biggest green impact. The problem for venture capital with some early technology stuff is that the projects do not fit. They have the potential for a big green impact, but they are hugely risky. If we went out and made 10 investments in early-stage technologies that might provide great opportunities in seven, eight or nine years and half of those failed, we would be sitting in front of you explaining how we have lost money and be unable to demonstrate to you that the projects that were still going would deliver, because they would be very early-stage projects. What that would demonstrate to the market is that this renewable energy stuff is all quite difficult and very risky and so perhaps it should not put any money into it.

However, we are trying to demonstrate to the market that there is an opportunity on the infrastructure side, given the scale that is needed in the UK, to make good returns at low risk. If we can demonstrate that we can do that, then much more capital will flow in. That relates to your earlier point about not having enough capital. Some of that capital will flow in directly on the back of good results from us. Some of it may flow in to us because people might say, “You guys are doing a great job. Can we put some money alongside your money and then we’ll have much more capital?” We would therefore get a virtuous circle. However, the other side is that you could be out of work in three months.

Lord Smith: Incidentally, we have lots of foreign investors, such as sovereign wealth funds, talking to us all the time and asking, “Can we get in on this action?” There is no shortage of capital out there.

Shaun Kingsbury: Short answer on interconnectors: great idea.

Mike MacKenzie: I hope that you will look at that area very carefully.

It seems to me that you want what everybody else wants: low risk and steady, moderate success. For new technology, though, with its exciting possibilities, everybody is standing by hoping that the other guy will do the pioneering work. It seems to me that to really make a difference somebody has to go first. Perhaps it is not you; maybe it will be somebody else.

Lord Smith: It is very frustrating. I spent 40 years in the venture capital industry, so I am desperate to do that work.

The Convener: Two members want to ask what I hope will be very brief supplementary questions.

Marco Biagi: If you return a profit on your capital, would you expect to be privatised?

Shaun Kingsbury: I guess that over time our job is to crowd in and capitalise private sector investment. That will be people who will co-invest with us and it may be done project by project. They may ask us to manage their money to find projects and they may put equity money into the bank. I guess all those things are on the table and it is up to our shareholder to decide when is the right time and who the right investors would be. However, if we are successful, I think that Government has a view that maybe they are not always the best investor in a commercial enterprise and we are a for-profits bank.

Lord Smith: It would free us from a lot of Brussels restrictions, because there are things that we absolutely could do—some of the venture stuff and stuff in other areas—that we currently cannot do.

Dennis Robertson: Coming full circle back to the pipeline projects—[*Laughter*.]

Lord Smith: Have you got one for us?

Dennis Robertson: I acknowledge your reference to the confidentiality aspect, but how many projects are based in Scotland and what is the forecast for investment?

Rob Cormie: It is very hard to give you a number for projects in the pipeline. The Scottish green investment portfolio's list shows that there are a couple of thousand. That ranges from tiny projects to very large ones, such as the big offshore projects in the Moray Firth and elsewhere. All we can say is that the investment banking teams across all the sectors have some very significant projects that we are working on as we speak. However, for confidentiality reasons, we cannot talk about them.

Dennis Robertson: But specifically with reference to the Green Investment Bank, I am just trying to ascertain how many projects will potentially be based in Scotland and what your investment forecast might be.

Rob Cormie: Do you want to know whether I can give you a number? I do not think that I can, because that is not the basis on which we operate. We are trying to create numerous opportunities and put them through a process to determine whether they are green and profitable, and that is it.

Shaun Kingsbury: If I may be so bold, can I give you a challenge? Street lighting here in Scotland is a tremendous opportunity. Payback periods are seven or eight years, technology is proven and each of you has some influence with your local authorities. Please help them to bring forward projects that we can finance.

The Convener: To follow up Dennis Robertson's question, I appreciate that you cannot give details of projects, but do you have a rough idea of what percentage of the £4 billion that you are talking about might be Scottish?

Shaun Kingsbury: Can we come back in writing, rather than guess at the number? We can give a range of how many projects there are, and their size, and we can write to you when we have had time to analyse that.

The Convener: That would be very helpful. Thank you.

Hanzala Malik: Until recently, we manufactured the wind farm equipment in Scotland, but it is no longer being manufactured here. Given the fact that we are looking for wind farms all around the country, and elsewhere, would you encourage that manufacturing to be re-established in Scotland if you had a proposal?

Shaun Kingsbury: The Department for Business, Innovation and Skills recently published an offshore wind strategy document. We fed into that and participated in a number of the workshops that the department held, to talk about how, for any wind farm constructed in the UK, we can ensure that a larger percentage of it is home-grown.

We would love to see the supply chain emerge, the key to which is seeing a long-dated list of investable projects. The first part of that is getting the CFDs, or contracts for difference, right, and getting the strike price right so that they are profitable. When we see the pipeline coming to fruition, with a five-year or 10-year track for building multiple offshore wind farms, the supply chain will begin to be invested here in the UK, because it makes sense to do it and it could be cheaper than bringing components from mainland Europe. What we need is a long-dated pipeline of those things to get the industry established, and we would support that.

Lord Smith: That is the nightmare scenario. We have wind, wave and tide, and that should be seen as a form of gold, like the North Sea. If foreign companies come in with foreign workers, they bring in the kit—the blades and whatever else—and erect them, and they carry on with the operation and maintenance of those farms and sell us back the electricity that has been made from our wind and wave.

By the way, I did not respond to what Hanzala Malik said earlier about Glasgow being the centre of the universe, because some of these guys do not come from Glasgow.

Hanzala Malik: No, but they need to know.

The Convener: I think that we need to call it a day. I thank Lord Smith, Mr Kingsbury and Mr Cormie for coming along. It has been a helpful session. It has run a little bit longer than we anticipated, but that reflects the number of issues and the interest of committee members in the subject. We would like to continue a dialogue and maybe get you back before the committee in a year's time for a progress report.

11:23

Meeting suspended.

11:28

On resuming—

Bannockburn 2014

The Convener: Item 4 is a response from Fergus Ewing at the Scottish Government to the committee's report on Bannockburn 2014.

As members will be aware, VisitScotland and the National Trust for Scotland have already undertaken to come back to us in January for a further evidence session and an opportunity to update the committee on how things are progressing, not just in relation to Bannockburn but in relation to the year of homecoming 2014. That will be a useful opportunity to question witnesses on issues such as ticket sales and how events planning is going.

Do members have any comments on the minister's response? Do we want to take further action, or are we happy to wait until the next evidence session? I am happy to note any suggestions for that evidence session. Are we all agreed?

Members *indicated agreement*.

Hanzala Malik: Do we not normally write to ministers to thank them for responding to us?

The Convener: I do not think that we routinely thank ministers for letters, but we always express our gratitude to Mr Ewing in fulsome terms when he comes to the committee.

Hanzala Malik: I am quite happy to thank him then.

The Convener: We shall pass that on.

"Low Carbon Scotland: Meeting our Emissions Reduction Targets 2013-2027"

11:29

The Convener: We move to item 5. The Scottish Government has provided a response to the committee's recent report on the second climate change report on proposals and policies—RPP2—which we have before us, along with supplementary evidence from Professor Sean Smith of Edinburgh Napier University and from Stop Climate Chaos Scotland and WWF Scotland.

We have a number of options—for example, we can go back to the Scottish Government on a number of issues. First, do members have any comments on the Government's response or any issues that they wish to raise?

Alison Johnstone: I am happy to wait until we come to our consideration of Professor Sean Smith's response.

The Convener: We are there now.

Alison Johnstone: Okay. At paragraph 3 of his submission, Professor Smith states:

> "I wish to see abatement measures met and achieved and my research institute works closely to deliver new methods and measure effectiveness. However, these RPP2 values are without foundation and the Chair of the EET should request that they are removed, otherwise the RPP2 becomes a document of 'smoke and mirrors'."

Would you consider doing that, convener?

The Convener: I am entirely in the committee's hands on that matter. Professor Smith raised that issue when he gave evidence to the committee, and we had an extended discussion about it at the time. He is referring to the additional technical potential in the figures for abatement in domestic dwellings. His evidence was very strong, and he said that it is just basically a made-up figure—a balancing figure, in accountancy terms—and that we do not know where that additional potential will come from.

If members want to pursue that further, we can do so. Are there any other views?

Mike MacKenzie: I take the points that Professor Smith and Alison Johnstone have made. However, we have fast-moving technologies that may give us a better understanding of what we can do—to improve domestic energy efficiency, for instance—and so we cannot look into our crystal ball and know exactly what the solutions are.

We can, to a certain extent, set a target that is both challenging and achievable, and that explains the figures. After all, the minister will really catch it—not least from you, convener, I suspect—if the targets are not met. There is a trade-off in setting a challenging target, which by its nature will not be easy, and we cannot necessarily know exactly how we will meet it. That is what Sean Smith is on about. With current technology, it is difficult to see exactly how the figure arises, but I do not think that it is anything to worry about.

Chic Brodie: I have a slight concern about Sean Smith's supplementary evidence, on which Mike MacKenzie has commented. The evidence is worthy, but it seems to be saying, "Those measures are rubbish—and, by the way, I am coming up with a new method of working and I have applied for funding." That really does not help his cause.

Mike MacKenzie: Or maybe it does.

Chic Brodie: Well, in my view, it does not help his cause. If he had included some historical evidence to say, "These were the targets that were set and, on the basis of the information that we currently have, they are rubbish", it might have been better than saying, "They are rubbish—and, by the way, I have new methods and I am looking for a grant from the Scottish funding council to set up a team of experts." I wish him the best of luck, but he really has not helped his cause.

The Convener: That is something of an ad hominem attack on Professor Smith.

Chic Brodie: As usual, I said at the beginning that his evidence was worthy, but there we are.

Marco Biagi: The technical annex to the initial draft RPP2 referred to an in-house modelling exercise by the Scottish Government, which I believe was also mentioned in oral evidence to the committee.

We may simply have a difference of opinion between experts, which always happens—the collective noun for academics is "a disagreement"—and, on that basis, we have come to a position. We definitely need to look at that area, which has presented itself as an issue to be kept under watch.

The scale of the emissions reductions that are credited to that additional technical potential is significant, but that applies to the late stage. I do not see the need to use the sort of language that appears in Professor Smith's submission to describe RPP2 at this stage.

The Convener: There are a number of routes that we can take. We could do nothing, or we could ask the Scottish Government for a response to Professor Smith's fresh evidence.

Mike MacKenzie: Why do we not write to the Scottish Government and ask for its response?

The Convener: Are members content to write to the Scottish Government to say that Professor Smith has given us supplementary evidence and to ask for its opinion on that?

Alison Johnstone: Yes.

Chic Brodie: Can we ask the Government not simply for a reaction but for a response that is supported by information from its technical people on how the measures are produced?

The Convener: Yes, we can do that. Are members content with that approach?

Members *indicated agreement.*

The Convener: Does anyone want to raise anything else regarding the Government's response to RPP2 or the other evidence that we have received?

Marco Biagi: I welcome the fact that all the things that we asked for—such as better information and clarity—were included in the final draft of RPP2. It is easy for us, as a committee, to complain when things that we ask for are not done, but when they are, due thanks is appropriate. I am not suggesting that we write to thank the Government, but I wanted to put that on the record.

Alison Johnstone: I find it quite heartening that Professor Smith has felt able to state his views very clearly and then say that he would like funding for another project. It would be less than honest for him to hold his views back and come at us and say, "I'd like funding for another project." Such honesty is admirable.

Chic Brodie: I take your point, but it would be more helpful if he had said, "I wish to see the abatement measures met, and here is why I think our measurements will be better", rather than saying, "These are not good—and by the way, I am now looking for funding."

Alison Johnstone: I do not think that he is saying that they are not good. He is simply saying, "What are they?" Frankly, I do not want to rely on a crystal ball to work out how we will meet our climate change targets, but I think that he is saying that they are being missed and that there is no suggestion as to what those abatement measures are.

Chic Brodie: I accept that, but he says that they are without foundation. I would like to have seen an explanation of why that is the case, instead of what he has said. I say good luck to him—I hope that he gets the funding that would allow him to do whatever he wants to do—but it would have been fairer to say, "They are without foundation, and here are the reasons why."

The Convener: To be fair, when Professor Smith originally gave evidence he was quite clear about why he felt that they were without foundation. He felt that the idea of additional technical developments that would allow the gap to be met was a very nebulous concept.

Anyway, I think that we have agreed on a course of action, so, rather than pursuing that debate, we will move on to a number of other issues that are in the paper that members have before them.

I would be happy to request that the Scottish Government keeps us informed of its progress in delivering on RPP2. Do members wish to request an update on the conclusions of the Sullivan panel, which relates to home insulation?

Mike MacKenzie: Yes—that might inform our discussion regarding Sean Smith's concerns.

The Convener: Okay. Are we happy to consider the funding of climate change measures that are set out in RPP2 as part of our budget scrutiny?

Members *indicated agreement.*

The Convener: We can keep a watching brief on the issue of the energy company obligation and the green deal energy efficiency schemes in Scotland. That will come up in the budget scrutiny, but we will want to keep an eye on it. We can consider Scotland's progress in meeting emissions targets when the next annual target report is produced in summer or autumn of 2014.

Do members agree to that?

Members *indicated agreement.*

The Convener: Thank you. With that, we move into private session.

11:40

Meeting continued in private until 11:56.

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