Sparking revolution in European energy policy

By Peter Nolan
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ENERGY stands at the top of the policy agenda in Europe. The European Commission considers the liberalisation of electricity and gas markets to be a key part of what it calls the Lisbon agenda, its laudable if unlikely goal of making the European Union "the world's most dynamic and competitive economy" by 2010.

But wrong-headed policies are still obstructing market solutions for energy, with predictably disastrous results for consumers – compounding high oil prices, Russia's gas imperialism and instability in the Middle East.

"Power Failure: The Politics of Energy in Western Europe", a report I co-edited with Sacha Kumaria for the Stockholm Network, examines the state of energy markets in six EU member states – Britain, France, Germany, Spain, Italy and Ireland.

Since the election of the Thatcher government in 1979, Britain has been the pioneer of such liberalisation. Thanks to privatisation, deregulation, freedom of inward investment and strong, independent regulatory bodies, the UK has enjoyed consistently falling prices for consumers.

By December 2005, nearly 11.7m (46%) and 9.3m (44%) of domestic electricity and gas consumers had chosen suppliers other than the incumbent former monopolies. More than 300,000 customers change their gas or electricity supplier each month. Once the sole monopoly, British Gas retains barely 50% market share. Over 1990-2004, according to energy regulator Ofgem, British households paid £75bn less than Italy for their gas, £67bn less than in Spain, £35bn less than France and £28bn less than Germany.

This has done wonders for Britain's competitiveness and attractiveness for foreign investors – and Europe, you might think, can have no better model for the EU energy market of the future. Nevertheless, despite three major internal market directives on energy, the latest promising all consumers freedom to choose their gas and electricity suppliers by July 2007, reform has been stymied by pressure from national governments and aggressive lobbying by the flabby incumbents, usually state-owned, in the electricity and gas industries throughout much of the rest of the EU. Competition commissioner Neelie Kroes has concluded that excess concentration among state-owned or state-favoured incumbents has led to higher prices. As Carlo Stagnaro of the Instituto Bruon Leoni points out in his study of the Italian market, the biggest problem is the divide between theoretical and actual liberalisation. While some legal obstacles to new market entrants have been removed, firms seeking to develop new energy capacity and infrastructure still often find themselves thwarted by an intricate web of regulatory barriers to entry, a common situation in the countries surveyed.

As its North Sea oil and gas fields begin to run dry, Britain has just become a net importer, exposing it for the first time to the less open and competitive gas markets of continental Europe. During the past winter, gas prices rocketed to record levels. Rather than export gas to Britain so as to take advantage of prices above those in their domestic markets, continental incumbents sat on their inventories. Angry British ministers and energy regulators have put the blame squarely on anti-competitive practices in European energy markets tolerated by other EU governments, and Chancellor Gordon Brown wants an investigation. State ownership also remains a significant obstacle to efficiency: most politicians, particularly under European systems of proportional representation, prefer kissing babies to changing things. Incumbents face little incentive to cut costs when consumers have no choice but to pay inflated prices.

Looking at Ireland, Constantin Gurdgiev of University College Dublin writes: "The average industrial wage in Ireland is about E33,500, or E15.54 per hour. For the Electricity Supply Board [the incumbent generator], the average wage stands at E95,000, or about E43 per hour, and reached E140,000 at one power station in Dublin." Governments also find themselves dependent on gas and electricity monopolies as a source of revenue rather than investing in infrastructure to ensure long-term profitability.

If energy producers competed in truly integrated markets for gas and electricity, multinational energy firms could benefit from economies of scale in purchasing. They would be able to maintain a diverse generating base, insulating customers from volatility in energy prices and weather. With more infrastructure to carry gas and electricity between different national markets, competition could come even to small markets. European governments are now examining new technologies for providing their citizens with cheap, clean and reliable energy – wind, tidal, biomass and solar power are all likely prospects. However, they would do well first to harness the proven power of the market.

Peter Nolan is energy and environment director at Irish think-tank the Freedom Institute