The View From Europe

By Loyola de Palacio

EUROPE'S ENERGY MARKETS have been opened for competition for commercial and industrial customers. By 2007, residential customers will join them.

Today, increased competition has transformed European markets. However, its energy market is not yet fully competitive. We face structural problems. National markets are still largely dominated by the incumbent electricity supplier. In the last few years, we have seen an increasing level of concentration of the industry.

Deficiencies on the infrastructure side are at the root of many of the dysfunctions. In many cases, existing interconnections between national systems are not fully accessible to all suppliers. In other cases, the capacity of existing interconnections is simply too small. This situation could prevent real cross-border competition.

Without a doubt, the main benefit already realized has been the gain in productivity of the utility sector, as shown in various studies. The gas and electricity sectors' excellent performance underlines the contribution of the market-opening approach to drive efficiency improvements in productivity and the potential contribution of these sectors to European economic growth.

Prices for large users have fallen by 15 percent in the last 10 years. For residential customers, they've been cut by 30 percent in several member states.

The key to the overall market structure is generation. Experience in the electricity market to date has shown there is a general tendency for integration between generation and supply companies to avoid risk. Where generation capacity is concentrated in the hands of one, or even a few companies, the real possibility of consumers switching suppliers will be limited. This may, in turn, affect the performance of the market, since companies will be able to keep prices higher without fear of losing their share of the market.

Like the United States, Europe will not be able to cope with future energy demands without a very important investment in capacity. According to our studies, with the expected increase of demand over the next 15 years, Europe will require additional capacity of 600 gigawatts. This means setting up a power station of 750 megawatts every week.

The introduction of competition has changed the investment climate for new power plants. Instead of being a central government decision, investment will now develop in response to price signals. When the gap between generation capacity and demand narrows, prices will rise, making new investment profitable.

The European Commission has proposed granting enough power to regulatory authorities, and requested that member states closely monitor the evolution of demand. If necessary, it may spur additional capacity investment efforts in infrastructure and use several tools to force the construction of new power plants.

Typically there is one transmission system operator in each member state, except for Germany, where there are several. Although much progress has already been made in terms of unbundling network operators and introducing regulated third-party access, there are still certain aspects that remain unsatisfactory. A fully independent transmission system operator is crucial for a well-functioning market.

The deficiencies in the grid coupled with the lack of spare capacity are other big risks we must overcome. We need to reinforce and invest in our grid and generation to face the increase of peak summer energy demand.

CHALLENGES ABOUND

We are not happy with the increasing level of concentration of the industry. We didn't open and liberalize the energy business to encourage mergers and acquisitions.

Turning to the environment, the implementation of the Kyoto Agreement has not been an easy task for the gas and electricity utilities. The energy market will need to develop in a manner consistent with the European Community's sustainability objectives. In excess of 7,000 megawatts of additional renewable and efficient generation capacities was added to the market recently. This represents more than 50 percent of new generation capacity added in 2003.

The energy sector in Europe benefits from holding forums where utilities, regulators, and legislators from different levels can meet and deal with commons problems to enhance fair competition and the overall efficiency of the energy sector.

Loyola de Palacio was European Union energy commissioner from 1999 to 2004. She wrote this piece in response to questions posed by EnergyBiz.

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BOLSTER GRID SECURITY

A group of energy and security experts have been brought together by the federal Department of Homeland Security to tighten security around the nation's transmission and distribution network.

The group will be charged with outlining what research must be undertaken and what policies enacted to make power lines more secure from possible terrorist assault. Ed Badalato, a member of the group, told United Press International that every effort must be undertaken to secure the grid, which is essential to American security.