

## Energy Transition: A Multifaceted Challenge for Europe

### 1<sup>st</sup> Symposium: The impact of changing energy patterns on EU competitiveness

#### - Report -

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Egmont – The Royal Institute for International Relations and the Development Group organised a symposium entitled 'The Impact of Changing Energy Patterns on EU Competitiveness' on the 30<sup>th</sup> of April 2014. The symposium took place within the framework of a series of events related to the multifaceted challenges of the EU energy transition towards a low-carbon economy which have been held in Brussels since 2011. It was the first of four events in the new 2014 series.

#### Keynote address: The European energy policy in a global context.



The keynote address was provided by Dominique Ristori, director-general at the European Commission's Directorate-General for Energy (DG Ener). He began by pointing out four important points to keep in mind when discussing the development of a European energy policy. Firstly, the main challenge is to combine urgent problems, such as the crisis between Russia and Ukraine, with the mid- and long-term issues, such as the 2030 climate and energy framework.

Secondly, it is important to integrate the new dynamics in the global energy market – particularly the growing energy demand from Asia and the increasing supply from the United States thanks to the shale gas revolution (50% of current US gas production). Thirdly, considering that 80% of greenhouse gas (GHG) emissions result from energy production and consumption, the energy policy will be a key aspect of the climate negotiations for a global climate agreement by 2015. Finally, the EU imports 54% of its energy consumption, costing more than €1 billion per day.

He then outlined key EU priorities, which integrate competitiveness, security of supply and sustainability aspects. Firstly, the EU should moderate its demand by acting more on energy efficiency, particularly in the building sector (representing 40% of energy consumption). In order to mobilise funds for this, the EU should stop regulating and develop new financial instruments in association with the banking sector. Then the EU should develop more indigenous energy sources. As long as the safety and environmental risks are taken into account, shale gas and nuclear power should be further considered. Considering the importance of coal in the EU and in the world, there is



an urgent need to develop clean coal technologies. Regarding renewables, an EU-wide binding target of at least 27% by 2030 has been proposed by the Commission. All these investments should take place under a market-based approach. Finally, the EU should diversify its energy sources based on credible projects, such as the Southern Gas Corridor. In this regard, the EU and its Member States should develop their bargaining power with third countries, which means speaking with a single voice.

### Session 1: What is the impact of changing patterns in energy markets on EU competitiveness?



Giovanni Brianza, head of strategic planning and M&A at Edison S.p.A., opened the first session by showing that EU labour and energy costs are higher than in other major trading countries such as the United States or China, limiting EU competitiveness. Then he explained that the EU's energy market and utilities are facing major challenges, namely stagnating demand, the penetration of renewables, pressure on nuclear sources and limited retail client value. However, there are opportunities to overcome this situation both in the gas and power markets. In order to enhance gas competitiveness, EU utilities may tackle a window of opportunity for supplier diversification, as long-term contracts will progressively expire. However, new import infrastructures will have to be developed first. In the power business, EU utilities should consider exploring other options to enhance value creation in the three main sectors of the energy system. In the generation sector, they should invest in renewables and exploit capacity markets. Although support for renewables has contributed to increased energy costs, renewables are likely to continue to grow thanks to technological improvements and related cost reduction. In the transport sector, new infrastructures and services should be developed. In the retail sector, utilities should consider the customers as the main asset and focus their strategy on energy efficiency and retail services.

Afterwards, Baudouin Kelecom, Fuels Executive for Refining & Supply Planning at ExxonMobil, started by recalling that, although we can expect a significant shift in the energy mix, oil will remain essential for European economies for the foreseeable future. The refining industry is an essential and integral part of many other European industries. However, with the dieselisation of demand, the EU refining industry needs to export gasoline and import diesel. This growing regional supply/demand imbalance and the new export capacities in the Middle East and Asia have led to record low utilisation of European refineries. He also underlined the competitive advantage of the US industry, where electricity prices are two times lower and gas prices are three times lower than those in the EU. Then he explained that Europe's current regulatory environment is having a cumulative impact on Refining, affecting the industry's competitiveness compared to other regions. Finally, he said that EU policymakers can help European competitiveness by encouraging market conditions that provide European industry with access to energy and feedstock at a competitive cost and by adopting transparent, predictable and market-based policies.



Next, Inge Bernaerts, head of wholesale markets, electricity and gas at the DG Ener, presented the main findings of the Commission's energy prices report. She started by demonstrating how retail prices of electricity and, to a lesser extent, gas rose under the influence of market forces and government policies (mainly related to decarbonisation) by up to 4% a year between 2008 and 2012 (above inflation). The price differences across Member States are large in retail electricity and gas across markets and have increased over time. The energy and gas retail prices are composed of three main components. Taxes and levies and, to a smaller extent, network costs are the two main components responsible for the increase in electricity and gas prices for both households and industries. Regarding the commodity component, electricity and gas prices have slightly increased for households, while they have decreased for industry. Then she explained that there is a disconnect between convergent wholesale markets and diverging national retail markets. However, the convergence and fall in wholesale electricity prices has not resulted in lower retail prices. Therefore the completion of the internal energy market through interconnections of smart networks is one of the instruments the EU has at its disposal to ensure the competitiveness of energy prices, alongside other policies such as energy efficiency and diversification of sources of supply. Finally, she stressed that the energy price gap between the EU and major economic partners has increased in recent years.

Lastly, as discussant, Jayesh Parmar, partner in Energy Advisory Services at Baringa Partners, started by explaining that due to international competition, there have been quite a few repatriations of industries to the United States. Those decisions are not taken lightly as repatriations are expensive. However, companies base their investment decisions on the fact that the price differential between the United States and the EU is a sustained trend. He also explained that one of the issues with completing the internal energy market is that we are still tied in with incentives around decarbonisation and relatively targeted investments, which are still very different from one Member State to another.



## **Session 2: How to handle and mitigate the impact of high energy costs on EU competitiveness.**



Matthew Gordon, director for EMEA Government Relations at Honeywell Europe, began the second session by stressing that the first priority should be to do more with less by using energy efficiency, instead of focusing on energy costs. Policies can no longer be based on supply only – demand is also key. In the old system, the challenge was to manage supply to suit demand, whereas in the new system the challenge will be to manage demand to suit the available supply. Thanks to an energy system

balanced between generation, storage and demand management, the volatility of supply is matched by the variability of demand. In order to achieve this, we need active and engaged consumers who understand why using energy at different times is important. Demand management requires disruptive technology for generators but un-intrusive technology for buildings that is unnoticeable to the occupants. He also stressed that energy efficiency targets are necessary in order to engage people, before concluding by explaining the numerous benefits of using less: reduction of carbon, imports and cables in the ground, but also increased energy security and profitability.

Following Mr Gordon's presentation, Wolfram Vogel, director of public affairs and communications for European Power Exchange - EPEX Spot SE, gave a presentation explaining why power exchanges and market coupling are tools for mitigating energy costs, favouring EU competitiveness. He started by reminding the audience that the power exchange centralises the buy and sell orders of energy professionals. The power exchange thus promotes the emergence of a transparent, regular, fair and neutral market price. The power exchange is separated between day-ahead markets, which optimise liquidity via blind auction and without price indication in the short term, and intraday markets, which are more flexible thanks to a continuous price formation in near real time. These spot markets serve as price references. EPEX Spot's markets represent 40% of the EU's integrated electricity market. The integration of European power markets thus has an inherent incentive. This process is supported by harmonised cross-border trading systems. The objective is to integrate the EU electricity market by the end of 2014. This is being done via European market coupling that offers many benefits: the facilitation of congestion management, price convergence of market areas, the absorption of extreme weather conditions across several market areas, a smoothing effect on negative or positive price spikes and a higher security of supply.



Afterwards, Alexandre Affre, director of industrial affairs at BusinessEurope, started by outlining four main lessons learned from the implementation of the 2020 framework, namely: (1) the importance of the impact of high energy prices on EU competitiveness; (2) the lack of coherence between EU policies and instruments; (3) the lack of coordination between the different national policies and the lack of political will to integrate the market further, and (4) the insufficient progress towards a global climate agreement. Then he recognised that although the diagnosis is established, the solutions are still missing and they will not be easy ones. In the framework of the adoption of the next 2030 framework, he stated the six main recommendations of BusinessEurope, which are: (1) putting cost-competitiveness, security of supply and climate objectives on an equal footing; (2) setting a single emissions reduction target; (3) tackling the question of energy efficiency with a sectoral approach; (4) maintaining the ETS as the main instrument – although it must be reformed, taking into account compensation mechanisms for industries exposed to competitiveness; (5) phasing out support for the market deployment of renewable energy sources, and (6) diversifying the EU's energy supply sources.

Finally, as discussant, Claude Mandil, board member of the SBC Energy Institute and former executive director of the International Energy Agency, underlined the first way to mitigate the consequences of high energy prices: the reduction of energy costs. In order to do so, we have to let the market work and deliver least-cost options. He also suggested the creation of a European independent regulator that would manage the internal energy market. As to the question of improving coordination among Member States – which are still sovereign on many important components of the energy policies – the answer was that a mandatory process of consultation should be established and organised by the Commission between Member States before national decisions are taken.



**Concluding remarks: How can the 2030 energy and climate package foster EU competitiveness?**



To conclude this symposium, Sandrine Dixon-Declève, director of the Prince of Wales' EU Corporate Leaders Group and executive director of the Green Growth Group, enumerated some of the reflections of the Business Green Growth Group for the 2030 package. These included concerns that (1) the issue of the EU's high energy prices is directed at its ambitions on climate change, while the main factor – the high cost of imported energy – is ignored, (2) long-term policy stability and short-term policy clarity are needed for industry and investor, (3) a two-track approach, which protects short-term competitiveness while ensuring long-term growth, must be followed, and (4) a target of at least 40% emissions reduction is the most cost-effective way forward. Then she highlighted the counter-productive economic outcome of avoiding ambitious low-carbon actions. According to the IEA, every year of delayed mitigation action adds €500 billion to the global low-carbon energy investment bill between 2010 and 2030. Furthermore, she stated that the EU is the low carbon market leader with 22% of the global low carbon and environmental business market (over €900 billion p/a), 35% of global low carbon patents and 7.8 million people employed in one million companies. However, the EU risks losing its leadership, as its global investment share decreased from 40% in 2009 to just 29% in 2012.

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