

Electricity Liberalisation in the European Union: A Progress Report

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It is around 5 years since my colleague, Tooraj Jamasb, and I reviewed the EU's progress with electricity reform (Jamasb and Pollitt, 2005). At that time many countries were still struggling to implement elements of the EU wide policy on electricity sector liberalisation that they had signed up to. Five years on, it is a good time to revisit the issue of how successful this wide ranging set of policies have been and to assess prospects going forward.

In this short update paper we review the latest evidence on progress with electricity liberalisation in the EU. We begin with a short review of the legislative background. We continue with a look at the evolution of markets and trading in electricity across the EU. Next we outline progress with the key reform elements and their impact on market structure issues within the EU. We look at the performance of the whole sector and company level performance. We proceed to discuss progress in reducing emissions and promoting renewables. In closing we note recent developments in electricity reform.

It is difficult to briefly summarise the result of a simultaneous economic policy experiment carried out across 27 countries. While some European countries have made substantial progress towards competitive electricity markets (e.g. the UK, Sweden and Finland), others have some way to go (e.g. France and Germany). However there are a number of general conclusions that may usefully be drawn at this stage.

First, there has been an impressive forcing effect of successive EU electricity directives. Market opening has proceeded rapidly across the EU. There has been a standardisation of market rules and

regulation and widespread acceptance of what constitutes best practice.

Second, there have been some notable market impacts. These include significantly increased EU cross-border trade in electricity, improvements in the quality of regulation, impressive labour productivity gains, some price falls (relative to the counterfactual) and a degree of price convergence.

Third, the market remains incomplete and significant competitive concerns have been identified by the European Commission. Prices have risen and diverged since 2003 and there seems to be continuing market power being exercised by incumbents and concerns that mergers may be increasing this.

Fourth, a positive social cost benefit analysis of reforms at the EU level is still difficult to call. Consumers were seeing lower prices and convergence but this trend has been partially reversed. Profits of EU electricity firms have not suffered unduly due to the introduction of competition. The impact on government in terms of increased government efficiency, reduced subsidy and improved tax revenue is not clear, but there is no clear evidence that governments have suffered welfare losses due to electricity reforms.

Fifth, significant new challenges to the liberalisation agenda have emerged. These include concerns about security of supply both as a result of rising quantities of intermittent renewables on the system and also about the reliability of Russian gas deliveries to the EU (following Russia's gas disputes with Ukraine) and hence whether 'energy security' should be left to the market. Challenges also arise from an ambitious EU climate change policy and its requirement to move towards rapid decarbonisation of the electricity sector. This has raised issues of whether national support mechanisms for low carbon generation can be made to mesh with a competitive wholesale electricity market.

Finally, high commodity prices and the rising costs of renewables have raised issues of energy poverty and the extent to which governments need to intervene in the pricing of residential electricity to protect poor consumers.

In closing we ask what might the next five years of EU electricity market development bring? Will liberalisation continue to advance or will it go into reverse?



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