

States and Markets in the Energy Sector

Dieter Helm

Professor of Energy Policy, University Oxford

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1. What is the scale of the problem?
2. What is the role of governments in energy markets?
3. What is the role and limits of competition?
4. How can security of supply be improved?
5. Is TPA, transit and open access to pipelines desirable?
6. What should the next steps in European energy policy be?

1. What is the scale of the problem?

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For security of supply:

- Global nationalisation of oil and gas reserves
- State-sponsored producer monopoly model now the norm
- Dash-for-gas in Europe (and elsewhere) increases import dependency

For Climate change:

- China +1000 GW new coal plant by 2030
- Global CO₂ ↑ c.50-60% by 2030
- World population 6 → 9 billion by 2050

⇒ MAJOR ECONOMIC AND POLITICAL CHALLENGE

2. What is the role of governments?

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- Market failures are *multiple* and *extensive*
 - complementarity
 - externalities
 - sunk costs
 - market power
 - depletion of resources and optimality over time
- Security of supply is a *system* property - and a public good
- Climate change is a *global* public bad

⇒ EXTENSIVE INTERVENTION

3. What is the role and limits of competition?

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- Competition is a *means* not an *end*
- Competition cannot provide optimum networks and security of supply
- Competition is not spontaneous - regulation for competition essential element
- Liberalisation is not the same thing as competition
- Liberalisation tends to spot contracting - not long term contracts

⇒ COMPETITION *WITHIN* A POLICY FRAMEWORK

4. How can security of supply be ensured?

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- Networks require top-down planning
- Completing European grids has significant pay-offs
 - national support
 - portfolio margin reductions
 - increases competition
- Networks require regulation to protect investors and pass through costs via use-of-system tax base
- Capacity markets to price insurance
- Strategic storage (and auctions) for gas
- Common regulatory position for upstream monopsony

5. Is TPA, transit and open access to pipelines desirable?

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- From the producer perspective:
 - upstream sunk costs in fields and power stations
 - depletion policy
 - control of flows for storage etc.
 - pipeline control
 - maximising downstream rents
 - maximising flexibility in system
- From the consumer perspective:
 - minimising upstream market power
 - leads to spot pricing
 - ambiguous effects on security of supply

⇒ British Gas monopoly structure and Gazprom approaches similar and rational

⇒ Transit, contract form and arbitration

6. What should the next steps in European energy policy be?

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- Priorities should be:
 - complete internal physical networks
 - mutual support arrangements
 - strategic gas storage
 - common external regulators
 - new pipelines to Caspian
- But not:
 - attempt to persuade Russia to open up networks to TPA
 - break up long term contract incentives
- And perhaps:
 - to unbundle to create EU gridcos

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