

# Recommendations for a more effective energy market

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## **Since the liberalization of the energy sector in 1990, just 5 percent of Spaniards have switched to another electric company.**

Responsible consumption, usage-based metering, measures to mitigate market power, structural market reforms and regulatory stability are the keys to the future for Spain's energy sector. These are some of the conclusions to be drawn from the study "[Regulation and Competition in the Spanish Gas and Electricity Markets](#)," conducted by [Xavier Vives](#) and Giulio Federico of the [Public-Private Sector Research Center](#) at IESE, along with Natalia Fabra of Universidad Carlos III of Madrid.

The energy markets in Spain, both gas and electricity, are gradually improving. The entry of new operators in certain segments of the value chain - as seen in the wholesale commercialization of gas and electricity, and in the provision of gas on an industrial level - has translated into significant growth.

Nevertheless, public energy policies still run into numerous obstacles, namely the need to reconcile some rather disparate objectives, attending to environmental considerations and fostering competition both nationally and internationally.

Meanwhile, some critical issues remain outstanding in terms of competition and regulation of the sector: the combination of ineffective regulation and market concentration gives rise to imperfect competition.

The distorted application of both regulations and merger control adds artificial obstacles for the restructuring of the sector. There is an increasingly high level of dependence on imported

energy sources, especially gas. The process of liberalizing commercialization to private parties is slow-going. Moreover, a coherent policy must be developed to promote the proper combination of technology for generating energy in the medium and long terms.

## **The context**

The rise in fuel prices and consequent increase of electricity prices, coupled with the lack of competition in the sector, have sparked an intense debate in Europe as to how to improve regulation and achieve more effective competition in the energy industry. In addition, Europe currently has a strong dependence on imported gas, primarily from Russia, but also from other countries. This situation also affects Spain, especially due to the impact that the international price of oil has on imported gas.

The growing convergence of gas and electricity, particularly at the wholesale level, translates into increased competitiveness in both markets, but at the same time it means that price variations experienced by one will affect the other as well.

Spain also presents some structural problems, including a considerable growth in the demand for electricity, low levels of interconnection with other European countries and a high level of concentration. Furthermore, there are significant regulatory distortions for competition in the market.

However, there is a bright side to all of this. As noted by the authors, renewable energies such as wind power and, more recently, solar power, are seeing a considerable upswing. Spain is also seeing rapid expansion in the importation of liquid natural gas (LNG) and infrastructures related to re-gasification. As a result, Spain is becoming one of the European leaders in this area.

## **Recommendations**

The report offers five recommendations for stimulating the Spanish energy sector in the future:

1. *Promote a balanced combination of energies and energy demand management.* There is a need for greater diversification of energy sources - in other words, the continued backing of renewable energies, and increased efforts to encourage energy saving.
2. *Adjust the electricity rates for end users and inform consumers about correct market prices.* To avoid further escalation of the so-called tariff deficit, rates should be adjusted

according to market prices. This would additionally allow for a faster, more effective liberalization of the gas and electricity markets. For some time now, prices for the end consumer in Spain have been artificially lowered. This, in addition to the absence of time-of-use rates, has led to excessive demand and rendered the capacity of the existing installations insufficient.

3. *Offer policies to mitigate market power and make the sector more effective.* One example of these measures, introduced by the government and aimed at suppliers, would be to offer longer contracts for virtual power plants (VPP).

4. *Promote an efficient business and market structure.* Artificial impediments should be eliminated, at both the legal and regulatory levels. This would give the sector the opportunity to have efficient corporate restructurings take place and respond to both technology and market trends.

5. *Improve regulatory stability.* Promoting stability in this area in the long term would avoid the current uncertainty regarding many aspects. For instance, merger control is not applied on a consistent basis. Moreover, policies on regulated electricity rates should be geared toward achieving a more competitive and efficient energy market, and not toward controlling inflation.

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