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Comments on "Energy Sector Competition Policy"

Douglas Brooks[1]

Key elements of trade in energy services are (1) that it is often difficult to separate the service component from the goods involved in supplying that service; (2) that the natural monopoly characteristics of energy service provision mean there is a critical role for competition policy in the sector; and (3) that energy is often viewed as a strategic industry, in which foreign competition (or foreign ownership of domestic provision) is not welcomed on an equal basis with domestic suppliers.

The role of energy trade in poverty reduction comes primarily through the use of energy to generate growth in general and to facilitate the provision of essential social services. Energy trade may also benefit the poor living in border areas not connected to the domestic electricity grid, or where they may be more easily or cheaply served from foreign sources. The poor may also benefit from environmental improvements arising from more rational or cleaner energy service production or provision.

To realize the potential benefits for the poor from energy trade, it is most important to increase competition in the sector to increase efficiency and lower costs of provision, especially in the domestic energy sector. In this process the unbundling of the different stages in energy delivery becomes critical, as does the sequencing of reforms. Increasing competition may also involve facilitating investment and innovation, including foreign investment and other forms of technology transfer. The use of subsidies (in developing countries these are primarily consumption subsidies) rarely works well in practice, and should be employed only if they are well-targeted and trade distortion effects are carefully considered. Realizing benefits for the poor may also involve diversification of energy sources and smoothing regional unevenness in supply within the country.

In the energy sectors of Asia we find increasing oil import dependency and growing electricity trade. Some countries both import and export the same (or similar) energy products. Consumer subsidies are not well targeted and sometimes lower prices below world market levels (this has been the case in China, India, Indonesia, Kazakstan, and Korea). ASEAN has a number of agreements to promote intra-regional energy trade, a broad policy commitment to provide and ASEAN power grid, and a trans-ASEAN gas pipeline project. The APEC Energy Working Group has facilitated information exchanges on electricity regulatory arrangements, tariff setting methodologies, and a guide on "best practice" principles on institutional and regulatory structures. Indonesia removed electricity production, transmission, and distribution from its "negative investment list," opening it to 100% foreign ownership. However, private producers

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[1] Principal Economist, Macroeconomics and Finance Research Division, Asian Development Bank (ADB). The views expressed herein are the views of the author and do not necessarily reflect the views or policies of the ADB or its Board of Directors or the governments they represent. ADB makes no representation concerning and does not guarantee the source originality, accuracy, completeness, or reliability of any statement, information, data, finding, interpretation, advice, opinion, or views presented.

must still sign a power purchase agreement with the state power utility and artificially low tariff levels make it unlikely the sector will attract much foreign investment. The People's Republic of China awarded a $12 billion natural gas contract to Australia in August, diversifying energy sources as demand grows, while Exxon recently initiated a $3 billion refinery joint venture with Sinopec.

In moving ahead toward greater energy trade in Asia, it will be important for the region's countries to learn from the mistakes of others (such as the perverse incentive structure that led to California's energy crisis, or the lack of transparency and reliability in wholesale energy pricing and reporting highlighted buy the Enron scandal). The importance of independent regulators, to avoid regulatory capture, should be stressed. One point which should be clarified is whether electricity distribution has characteristics of a natural monopoly, as transmission does. Most countries in Southeast Asia maintain monopoly power in distribution while other countries do not. To promote competition, it is essential to have a level playing field at least between government and private energy sectors. Finally, countries in the region should take advantage of support (from suppliers and possibly from bilateral and multilateral financial institutions for exploring alternative technologies and technology transfer opportunities, while keeping an eye on related environmental impacts.