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CRITICAL ASSESSMENT OF THE GENERATION SECTOR REFORMS IN THE NEW EU MEMBER COUNTRIES – A CASE STUDY

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OVERVIEW

In spring 2009, the Romanian government has proposed a new reform of the national energy sector to be implemented in the beginning of 2010. The reform involves the restructuring of the national power generation sector segment that is still owned by the state. As most of the power generation capacity is still state-owned, this reform will dramatically alter the competitive landscape of this sector.

In the previous phase of reform of the energy sector in Romania during early 2000s, several power generation companies owned by the state were created. The specificity of that reform phase was that all the companies were created based on the fuel used by the generating plants – thus, several companies with coal-only or fossil fuel-only generation units were created, as well as a hydropower-only company and a nuclear energy company. This has created major distortions in the market and an imbalanced competition, as the production costs of the different state companies ranged from 26 EUR/MWh (for Hidroelectrica) to 109 EUR/MWh for the worst-performing generation company [1]. In this context, the 2010 reform has as declared objectives to increase the energy supply security and create a sustainable power generation sector – according to the long-term national energy strategy [2]. Under the new structure in the reform proposal, two national power generation companies were to be created, with similar total production capacities, each of them being distributed a mix of various fuel generation assets from the former companies.

The proposed principles of the reform are: the use of a fuel mix in the new generation companies instead of a single fuel to increase the power supply security; development of a truly competitive Romanian power market; creation of a limited number of strong companies, capable of competing on the European market and to invest in new and clean technologies; maintaining the jobs in the traditional thermo power plants and in the coal-mining sector; and creation of several companies that have similar production costs and market share [1]. Based on these principles, several external assessments prepared during 2003-09 have proposed a series of 7 restructuring options and 14 scenarios. The criteria used to assess the different scenarios were: a balanced fuel mix, the level of market concentration post restructuring (measured by the Hirschmann-Herfindahl Index – HHI), the market share of the two new companies (post restructuring) and the average unitary production cost of the two new companies [1]. The government finally chose the scenario of two new large state companies plus several smaller producers – usually joint ventures between a state and a private company. The new structure presents some elements of vertical integration – by including one coal-mining state company and one power distribution state company in each new generation company.

This paper is analyzing the rationale and principles of the reform as stated by government documents and officials, the scenario methodology and criteria proposed by the government, as well as the proposed final outcome of the reform. Based on this critical assessment, we are able to make recommendations that can be considered for the continuation of the reform and for future similar cases in other countries.

METHODS

Complex descriptive study that uses both qualitative and quantitative methods

- Qualitative research methods:
    - Qualitative assessment of the reform principles, methodology and of the criteria used to give a rationale for the reform – market share, Hirschmann-Herfindahl Index, etc
    - Document analysis – in order to evaluate historical data and situations
- Quantitative research methods:
    - Descriptive statistics

RESULTS

While the rationale for the reform can be accepted, some of the reform principles are not relevant for the stated reform objectives – there is no final opinion on the issue of the ideal fuel mix -, are passive and past-oriented - focusing on the national market instead of the upcoming regional and European market, or simply populist – maintain jobs in certain sectors without any concern for their profitability.

Regarding the options listed by the external assessments, it is surprising that option D that would analyze the potential for regional generation structures (joint ventures with companies from other countries, etc) is mentioned, but not assessed, as it is deemed to be premature. More generally, all the options and scenarios are centred on the national power market, without comparing the new companies to similar regional or EU companies.

The criteria used for ranking the different scenarios are also controversial. The fuel mix criterion excludes the creation of any potential highly-profitable niche player. The use of the HHI index can be refuted from two points of view – the future of the power market is regional and European and not national; secondly, the HHI measurements for almost all the countries in the EU show that the national markets are all extremely concentrated and thus render the use of the index irrelevant. Moreover, according to the contestable markets theory, market concentration is disruptive only if the dominant players abuse their position [3]. The use of future national market share is also not relevant when we take into account the trends in the power market. Finally, the average unitary production cost criterion is not fair to the most competitive current companies, as they will have to cover the losses of the least competitive ones.

CONCLUSIONS

The 2010 reform tries to create national champions instead of future regional or European players. A more pragmatic reform approach – a “Realpolitik” energy reform - would create a company (or several companies) that would be able to take advantage of potential economies of scale or comparative advantages at a regional or European level. In other words, the outcome of a reform should be the creation of new generating companies that will either have the diversification, geographical coverage and critical mass to successfully compete against the existing large European and regional players or use a long-term competitive advantage to dominate very profitable market niches.

ABSTRACT REFERENCES

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