EU LIBERALIZATION POLICIES AND NATURAL GAS PRICES: UNDERSTANDING THE CURRENT ENERGY CRISIS

Roberto Cardinale
Department of Economics, School of Business
The American University in Cairo
Roberto.cardinale@aucegypt.edu

Overview

The recent surge of natural gas prices in the EU comes against the belief emerged in recent years of the definitive advent of an era of low energy prices. While agencies and analysts are attributing the causes mainly to a temporary convergence of unfavorable factors, this article identifies long-term structural and policy factors. This is done by exploring the causal relation between liberalization reforms and trends in gas supply in three major gas markets – UK, US, and EU. Through the lens of Transaction Cost Economics, the paper finds that although liberalization is effective for reducing prices in times of gas abundance, it might cause the opposite effect in times of scarcity. This suggests that the EU policy should contemplate the coexistence of models based on both market competition and vertical integration to take advantage from low spot prices in periods of abundance and contain the surge in periods of scarcity.

Methods

The paper adopts the methodology of the comparative case study (see Collier, 1993; Dion, 2003; Flick, 2006; Yin, 2009). The selection of the cases – UK, US, EU – follows Dion's (2003) creteria, which suggest that cases should be selected based on similarities on the variables to control for and on differences in the variables under investigation. In this paper, the countries selected have all mature and large natural gas markets, while more importantly, their liberalization reforms are in a advanced stage (comparing to other relevant gas markets worldwide). The variable under investigation is how the effectiveness of liberalization reforms (associated with low domestic gas prices) changes at different levels of domestic supply, with the EU being characterised by domestic scarcity, the US by abundance, and the UK having transitioned from abundance to scarcity.

Results

The UK, US and EU cases suggest that in conditions of gas oversupply, liberalization policies can successfully achieve the objectives of enhancing market competition and reducing final prices. However, it is necessary to clearly define the causal relationship between the two key factors – abundance of gas and infrastructure in relation to liberalization policies – and their respective influence on price reduction. In fact, the abundance of gas is an essential condition for the virtuous functioning of a competitive market. Without it, there would be no room for new competitors to increase their market share at the expense of established companies by offering lower prices to consumers.

Conclusions

The current worldwide surge in natural gas prices is hitting mainly import dependent countries, first and foremost in the EU. This comes against the belief emerged in recent years of the definitive advent of an era of low energy prices, brought about by increasing market competition and diversification towards renewables. The current supply shortage seems to have caught the EU unprepared and still in a transition stage in its path towards a more competitive and green energy market, suggesting that reforming the energy sector in the EU cannot overlook one of its defining features: the

persistence of a strong dependence from imports. Drawing from the experience of policy reforms adopted in the major world gas markets, the paper shows why liberalization is effective for reducing prices in periods of oversupply, while its benefits are offset in periods of shortage, such as the current one. The paper suggests immediate actions to overcome the current crisis and long-term policy directions to pursue price affordability and energy security.

References

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