

Making the internal electricity market work

Georg Zachmann explains why the economic pressure to create a comprehensive internal energy market is building

It is almost impossible to find a European policymaker who does not want a well-functioning internal energy market. And at first glance, the internal energy market does seem to be on track. In 2012, French and German power plants obtained the same hourly price for the electricity they sell 64% of the time.

Regulators and network companies are working at full steam to harmonise complex technical rules for cross-border electricity exchange. Co-ordination of the operation and planning of networks has substantially increased. So, completing the internal energy market next year – the ambitious political deadline set by European Union heads of state – seems feasible.

But all is not as it seems. Twenty years ago, the joint energy wholesale market was at the heart of the internal market agenda. This was sensible because competition between conventional power plants across Europe would improve operational efficiency, mean that consumers could be served by fewer plants and would reduce operators' ability to levy excessive prices.

But the energy landscape has changed dramatically. In 2012, 64% of newly installed EU electricity generation capacity was either wind or solar. The massive deployment of renewables makes electricity worthless when the zero-cost production from these sources exceeds the demand. In some countries, this is happening increasingly frequently with the deployment of renewables. As a result, in the second quarter of 2013, average wholesale prices in Germany, France, Austria and Switzerland fell below €0.03 per kilowatt hour (kWh), while domestic consumers in Germany continue to pay about €0.25/kWh.

At the same time, the value is



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increasing of more robust networks, flexible power generation capacity (for example gas turbines) that can quickly ramp up when renewables production is below expectation, and the capacity to produce electricity when demand is high and renewables production is low. The pricing of renewables, and remuneration for network availability, flexibility and capacity remains, however, organised nationally. National remuneration schemes have in many cases become less compatible. For example, capacity in France and Germany used to be remunerated through the wholesale price only. Now, France is putting in place a general mechanism to remunerate all capacity in its territory, while Germany has introduced a 'strategic reserve' that pays only for the capacities of selected power plants.

With incompatibility on the rise, the role of wholesale markets is bound to

vanish. Excess capacities and growing volumes of renewables that have no variable cost will cause the wholesale electricity price to converge towards zero. At the same time, electricity consumers will have to pay increasing levies and tariffs into the national schemes for remunerating networks, renewables, capacity and flexibility that are outside the internal market. Thus, the completion of the internal wholesale electricity market could be a hollow victory.

Internal energy market policy has to take this dramatic shift into account. A market design that remunerates bulk electricity, renewables, networks, flexibility and capacity consistently in all countries is the prerequisite for making the internal electricity market work. Coherent network planning is in the European public interest and should be organised and financed accordingly.

In a study for the European

Parliament, we showed that the benefits of deep integration can be substantial. A comprehensive internal market in which the conventional power plant fleets is optimised on the EU level, instead of nationally, can reduce the total system cost by 5%-10%. The benefits will be even greater if the roll-out of renewables, the provision of flexibility and network investments is optimised in a co-ordinated way.

So far, vested interests and concerns about national sovereignty have stalled the completion of the internal energy market. But, because the benefits of deep co-operation increase with the growing share of renewable sources of energy, the economic pressure to create a comprehensive internal energy market is building.

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Merkel can do well by doing good in Bosnia

Kurt Bassuener and Bodo Weber argue that Germany's newly re-elected chancellor has a chance to force progress in Bosnia, as she did in Kosovo

European politicians are beginning to wake up to the fact that Bosnia and Herzegovina is regressing and the European Union's policy is failing. But they have no clear ideas on what to do about it. Bosnia's political elites, a political-business-criminal nexus empowered by the Dayton agreement that ended Bosnia's civil war, have demonstrated that EU membership is much less appealing than remaining illicitly enriched, empowered, and unaccountable. This is not the way the 'enlargement perspective' is supposed to work. And since the EU has neutered the ability of the international community's high representative to defend the (admittedly deeply problematic) Dayton constitutional order, it has left

nobody else to blame.

Recent street protests triggered by a lack of political agreement on assigning personal identification numbers demonstrated deep dissatisfaction with the entire Bosnian political class. Sadly, these protests were not sustained. There remains a disconnect between the will of the majority of the population for accountable governance and forward movement toward EU membership and the activities of the ruling political elite, which is adhering to its more than 20-year-old playbook of attempting to stoke nationalist fears.

Yet the EU and other international actors, particularly the United States, are now airbrushing themselves out of the picture, taking no responsibility for creating an enabling environment for the Bosnian politicians who they rightly blame, but also continuing to propound the malicious fiction that citizens have actual leverage over their political elites. The fact is that the international community, and the EU in particular, has gone out of its way to legitimise Bosnia's warlord politics, meeting with political party oligarchs regularly in search of deals – any deals – which would allow them to claim

Potemkin progress.

EU officials point to the recent Serbia-Kosovo agreement as a victory for the EU's soft power. But had German Chancellor Angela Merkel not pressured then-Serbian President Boris Tadić in summer 2011 to solve the Kosovo issue or else forget the country's EU aspirations, the deal brokered by the EU's foreign policy chief, Catherine Ashton, never would have happened.

Germany will get more than its fair share of the bill if the situation in Bosnia continues to deteriorate. But contrary to its stance in the eurozone, Germany is impeding application of stronger financial conditionality on EU budget assistance and International Monetary Fund stand-by arrangements, to the irritation of many other northern members, and even France and Italy. The approach seems to be to keep refilling the proverbial bucket, rather than plugging the hole.

Now re-elected for a third term, Merkel has the opportunity to force a pivot in the EU and whole international approach toward Bosnia. As the centre of gravity of the EU, Germany can shape Bosnian policy. Merkel could declare publicly that

since Bosnian politicians obviously do not want to make the reforms needed to move toward the EU's open door, the Dayton order should continue – but now strictly enforced and without German taxpayers' assistance.

Practically, this would require reanimation of a credible international high representative (an office which should now be held by an American) and the EU military mission mandated by the UN.

This would create a whole new dynamic. Germany and other international creditors would cease to bankroll an inherently corrupt and corrosive system, indirectly encouraging citizens to confront their leaders. The EU's special envoy could assist by spelling out the actual costs of policy malpractice by political elites. By effectively tackling Bosnia, Merkel could portray herself as protecting Germany's economic and security interests.

The EU and West in general have reached a dead-end with the current policy toward Bosnia. Germany is best positioned to shift the policy. But can Merkel summon the will to do it?

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