Position paper
Energy Task Force

Liberalization and deregulation of gas prices

3 June 2014

Though it started late, Romania has made significant progress towards liberalizing its gas market. The wholesale price of local gas has now fully converged with Western European wholesale gas prices. Local gas does however remain less expensive than import of Russian gas. This import gas should nevertheless not be the reference price, as it would otherwise lead Romania to having higher gas prices than the rest of Europe.

Based on this analysis and as highlighted by the government, further increases of local gas prices, as initially agreed in the calendar approved by IMF/European Commission/World Bank, are no longer necessary.

To finalize market liberalization, a number of steps, such as the emergence of a real centralized wholesale market as well as the implementation of a modern network code and workable balancing rules, are still required. The main hurdle is the fact that experience in other countries has shown that the development of a liquid wholesale market that truly meets customer demands takes several years. The problem is even more complex in Romania as the supply of gas to the system is of highly oligopolistic nature, with basically only two local gas producers and one source of imports, ie. Russian gas. There is therefore a very high likelihood that, in the absence of a well tested and well functioning market, wholesale prices would immediately align on the level of the most expensive source, ie Russian gas, which is currently 30-40% more expensive than local gas and Western European wholesale gas. This would overwhelm the Romanian economy, jeopardize its sustainability and, in case of escalation of the Russian-Ukrainian crisis, even endanger the country's security of supply, as Romania can clearly not have yet a sustainable gas system without gas imports (and this should remain the case at least until the end of the decade).

If the target shall be to fully deregulate end-user prices, starting with industrial and commercial consumers, such deregulation cannot take place as long as there is no clear alternative in terms of supply, ie. a well functioning wholesale market, fed through a sufficient variety of sources and offering products and maturities that meet customer demands (such as year-ahead, quarter-ahead, month-ahead, week-ahead and not just day-ahead or spot trades, but also peak and not only base load). This is currently far from being the case, so that a deregulation at short notice of prices for the 170,000 industrial and commercial consumers impacted, that span across the whole economy and are currently still protected against market distortions through regulatory intervention, would most probably create massive chaos and unsettle the economy as a whole. A transition period of at least two years is therefore absolutely necessary. Regulated prices shall be maintained during this

transition period and of course also reflect true costs of market operators (for instance to cover the need to import for storage purposes in the summer and especially for delivery purposes during the winter, in order to avoid the risk of supply disruptions). In parallel, consumers should be encouraged to move to the free market through appropriate information campaigns, which does however also mean that the wholesale market will need to develop significantly during this transition period.

Coalitia is interacting well with the Ministry of Energy on this topic, but it is of utmost importance, to avoid chaos and unsustainable consequences on the economy, that Romania does not rush into decisions, whose impacts have not been properly assessed in all their dimensions and sufficiently thought-through beforehand. A gradual approach, which was also chosen by most European countries, especially those that rely on a very limited number of supply sources, would be the right and responsible one to adopt.

Any emergency ordinance that the government will need to adopt to adjust its existing gas legislation during the course of June should take those points into consideration.