

Liberalization of European Energy Markets

By Horst Michael Hanika*

Editors Note: The GEE hosted a very fine seminar in Berlin in early September on Energy Markets, What's New? at which Michael Hanika was the dinner speaker. His remarks, though light, are considerably to the point.

Mr. Chairman, Ladies and Gentlemen

It's in fact only a few hours ago when I heard, that I have to give a dinner speech. Dear Michael, I said to myself, say something substantial. This is my dilemma: all substantial things have already been said today. It was Winston Churchill, who was asked: "What makes a good speech?" And his answer was: "Well, you must have an attractive introduction, and an encouraging end. And all in between must be very short." That was my introduction, and I come to the center piece, which will indeed be very short.

This is the seventh conference on liberalized energy markets I have attended. And I could have participated in a dozen others, if I had had time. This indicates the degree of uncertainty we all have and the difficulties in drawing a clear picture on what the risks, the challenges and the opportunities are.

In search of solutions, almost everybody came to the same approach: have a look at already existing liberalized markets, thus prognosticating what will be happening here in the developing future energy markets in Europe, especially the biggest market in it, Germany. I congratulate everybody who has a clear picture, who knows what has to be done. However I call to your attention what the German philosopher Eduard Spranger said (this is known as "Sprangers Law") : "The outcome of our doings has always been different from our intentions."

Therefore, my thesis: We do not know what the liberalized energy markets will look like. However, we do know something, we have clear assumptions on the main trends and the main players. But still it appears to me and many others I know, that the future is well structured like a plate of spaghetti. Yes, of course, we have a legal framework, but the rest is market, and market is a chaotic process. This applies certainly to the energy markets, where we envisage rapid and fundamental changes. And let me, therefore, remind you of one important rule of chaos: a minimal change in the starting conditions can reverse the entire process: the butterfly phenomenon.

So, it's very significant, that this conference undertakes to restructure our spaghetti plate. Indeed, this is the first and only conference in which I have been participated, that also deals with corporate strategies and the only one, which has an emphasis on new technologies and renewables.

I'm very grateful for that, because this is exactly the problem, the ABB group has. However, there is a cloven hoof. When we talk about corporate strategies, we think it's the utilities strategies. But they are only a few of many players in this global game, if though the important ones. The utilities will face tough competition by new entrants: utilities from

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abroad, IPPs, independent marketers, wholesale traders and retailers, aggregators and other service providers. The cake is cut into pieces now, so everybody strives for a share. Fuel suppliers, IT-companies and engineering companies are well aware of their opportunities and not to forget the local municipal distributors, the Stadtwerke, they struggle, in order to survive. All of them have different goals and different strategies.

The possible strategies are numerous:

- One can focus on assets, single assets like power plants, grid, distribution, sales, gas, water, heat or be a multi-supplier.
- One can focus on information, such as traders, service providers, billing companies, stock exchange.
- And one can focus on the end customer, like IPPs and the municipal total service suppliers.

I fear, we still have a plate of spaghetti.

Now, what are the driving forces in this process? There are many, three of them are of paramount importance and you know them well: first it's money – prices, second it's money – cost, and third it's money - profits. Number 12 or so are environmental needs or technical necessities. That explains everything. At this time we still have a distribution system, now we are on the way to a customer market. And this has a number of effects:

- Prices will go down.
- Size becomes an important criterion. The utilities will grow by mergers or acquisitions.
- Electricity is only one form of energy. The customer asks for more. The utilities will diversify, also into fields like water and telecommunication.
- Everybody has to cut costs. Investments will drop, life cycle cost, maintenance, service will be reduced.
- Reserve capacities will be reduced.
- Cost driving power plants will be replaced by cheaper combined cycle gas fired and cogen plants and distributed resources.
- Renewable energies are interesting only in so far as they are competitive, which means for the time being, if they are subsidized – by whomsoever.
- New technical systems, such as distribution automation, dynamic loading, virtual power plants, remote services & repair and online metering will be welcome, under the condition, that they are useful for increasing competitiveness.
- Information technology will play a crucial role, because the amount of information grows by factors of 100. New software will be necessary for power plant control, system operations for grid stability, business management systems for metering, billing and trade.

Well, some people say all this threatening, risky, complex and complicated stuff is terrifying. I would say, it's fascinating. It's a great challenge, but first of all it's a great opportunity. Shouldn't we be grateful that we live in these fascinating times, grateful, that we can be navigators in these troubled waters? Just by having dinner in this marvellous place and talking to one another in a conference like this?

It's a wonderful time and I ask all of you: Let's have an optimistic look on our spaghetti plate.