

The End of the Energy Market Liberalization Era

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In the previous issue, I argued realistic and comprehensive climate change measures are necessary to regain the balance of 3Es. This time, I would like to consider economic efficiency in the present moment, when energy security has become a priority while the environment and economic efficiency are being sacrificed.

In energy policy, economic efficiency for a long time referred largely meant liberalizing domestic energy markets. The energy market liberalization began in the UK and US in the 1980s, as one part of so-called neoliberalism. The oil market had already been liberalized to quite an extent, and the majority of coal demand is for electricity power generation and steelmaking, so domestic energy market liberalization meant the abolition of monopolies in the electricity and gas businesses, and the unbundling of infrastructure sector (power transmission and distribution, gas transport and distribution). This was a lengthy process, and in Japan's case it took over 25 years, from the introduction of IPPs and liberalization of the large-volume gas market in 1995, to the full market liberalization of the electricity and gas retail markets in 2016 and 2017, through to the legal unbundling of nine power companies and three major gas companies in 2020 and 2022.

Ironically, just as the liberalization of energy markets at last ended, serious doubts are surfacing about the very rationality of liberalization itself. This is vividly illustrated in the EU. Immediately following the outbreak of the Ukraine war, subsidies were introduced for electricity and gas charges, a cap was set on the TFF price, a marker gas price, and there are plans to develop a new marker price. This means the liberalization of the gas market has ceased to function in Europe. In Japan also, subsidies were introduced for petroleum products from January 2022, and for electricity and city gas from January 2023 also. Additionally, energy companies unable to pass soaring fuel costs onto their retail prices due to supply contracts or regulatory restrictions are collapsing one after the other. It has not been

possible to bring about reductions in energy costs as a result of competition between operators, which was the outcome most hoped for at the start of liberalization. Consumers' options may well have widened, but a situation in which consumers seek refuge in final guaranteed supply contracts because new sector entrants are collapsing and new contracts are being suspended one after another is not what the liberalization aimed for.

The current energy crisis is directly attributable to the Ukraine war, but that is not to say this situation arose overnight. Investment in upstream oil and gas sector had been stagnating as a result of the pandemic and the net zero target. Furthermore, in Japan, even in the past, investment in electricity infrastructure such as power plants and transmission lines had not been adequate due to intensifying competition, and it had become difficult to conclude long-term LNG contracts. These factors too are contributing to the current electricity shortage and delays in new LNG projects. The fact that the Ukraine war broke out just as buffers for stable supply were being lost is making the current crisis a serious event. In other words, it may be that the liberalized energy market failed to take in externalities such as geopolitical risk and the environment.

To ensure stable supply and consistency with measures to address global warming, it is not as though policies of energy market fundamentalism have been adopted in Japan. Regulated prices remain in place for domestic electricity and gas charges, and unbundling has not gone as far as ownership unbundling either. Measures introduced in the electricity business in particular, such as FIT and FIP for promoting the introduction of renewable energy power generation, and the capacity market for adequate generation capacity, are undoubtedly examples of liberalization policies being amended from the standpoints of climate change measures and stable supply. However, it is also possible to argue that the more amendments such as FIT, the closer the energy regulation becomes to traditional cost plus method. The benefits and limitations of market liberalization should be closely examined in the future, but it is probably appropriate to view 2022 as the year that exposed the limits of energy market liberalization, and marked a shift to an era requiring more government intervention.