

# **Reforming Subsidies for Electricity Markets in the GCC**

## Session 2 – Dealing with Fuel Subsidies

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# What is a Subsidy?

- A subsidy is any **Government** support to bring the price of a commodity below its **market** price. 

- A recent paper from the Global Subsidies Initiative defined subsidy as “any form of preferred treatment granted to consumers or producers by a government” (based on the WTO’s approach).

- For the power sector it’s complicated because:



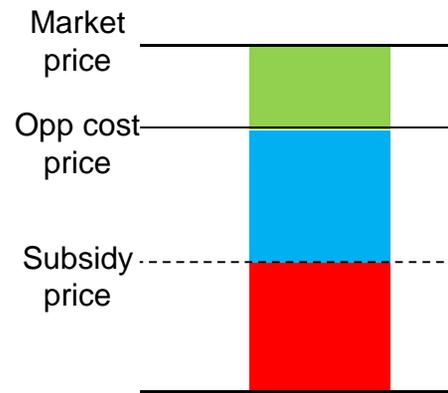
- Many policy makers consider fossil fuels even at market prices are subsidised, because their price does not capture their external (climate change) costs; and



- Many subsidies in the power sector are now paid to cover the extra costs of nuclear and renewable generation

# Defining the Problem

For today, the main issue is subsidies relative to “market” prices, or “opportunity cost” (where that is lower than the market price):



GCC countries are all in situations with significant levels of subsidy:

- The ME and N Africa region account for around 5.5% of the world’s population and around 48% of global energy subsidies
- Even on our definition of subsidy, all six GCC Member States have significant electricity price subsidies – in some cases consumer prices had not increased for many years
- Subsidies account for over 5% of GDP in most GCC states, and over 10% in some cases

# All MSs face subsidy issues (1)



Oman has operated significant consumer subsidies for some years, with:

- Subsidies provided through low fuel prices and subsidies in consumer prices paid for by Govt.
- Power sector entities allowed by AER to recover their full operation costs, compensated by Govt.

But recent years have seen significant developments:

- Gas prices for generation were doubled in Jan 2015, with planned annual indexation
- Some statements by policymakers suggest changes to consumer tariffs may cut the cost of subsidies

# All MSs face subsidy issues (2)



KSA has operated significant consumer subsidies for some years, but:

- No formal process for funding of the subsidies, though provision through a combination of low fuel prices, subsidised loans, and other credits to SEC from Govt.
- ECRA has no formal role in determining SEC's revenue requirement, so scale of subsidies not clear
- No published data on the scale of subsidies is available, but 2014 SEC accounts suggest that the average revenue per kWh sold is around 3.5 US cents

No recent changes have been noted, and there is no formal indication of any proposed changes to this position, but some commentators suggest that the pressure from lower global oil prices may result in a reduction in subsidies

# All MSs face subsidy issues (3)



Abu Dhabi has also operated significant subsidies for certain categories of consumers for some years, with:

- Government determining the consumer prices and making up the revenue shortfall of the distribution companies, based on RSB input

Recent years have seen significant developments:

- From January 2015, many categories of consumer electricity prices increased significantly
- From August 2015 fuel subsidies have also been reduced, including for transport use
- Some estimates suggest the total cost of electricity subsidies has fallen by more than 40%

# What about consumers?

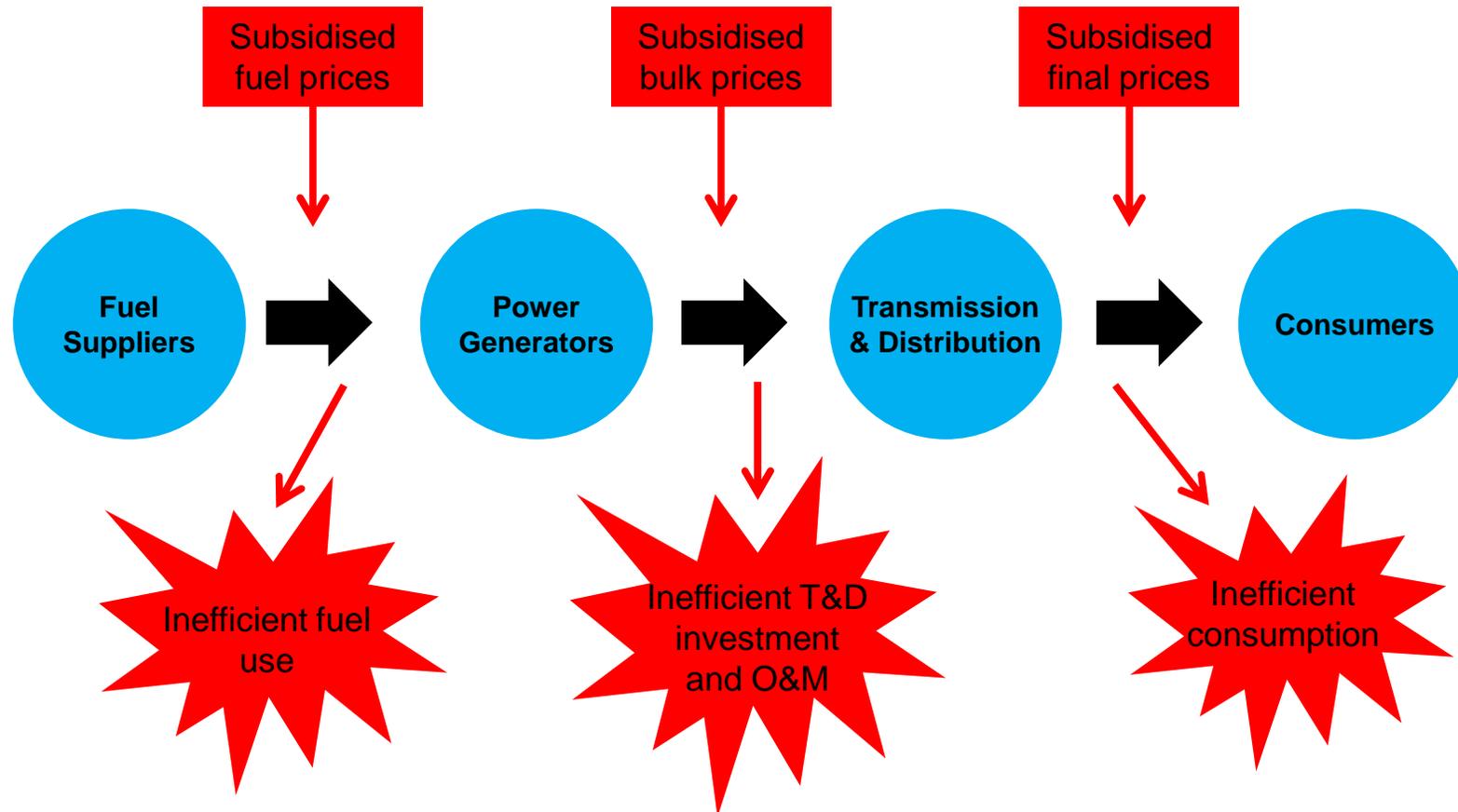


- Policies of providing direct electricity price subsidies to consumers are understandable.
- These subsidies may be intended as important elements of social and industrial policy, and may:
  - provide valuable aid to domestic consumers, especially vulnerable consumers;
  - aid small businesses to thrive and grow;
  - assist industrial development, especially energy-intensive industries
- But consumer subsidies are not the main issue here – though their reform is desirable

**The real issue is subsidies higher up the supply chain**

# The Electricity Supply Chain (1)

Even in a traditional power sector, subsidies can have adverse effects on all parts of the supply chain:





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