To the attention of EU Heads of State and Government
Cc: Member State Energy Ministers
Brussels, 10 October 2024

Subject: Draghi report on the future of European competitiveness– the European power sector is a big part of EU's growth story

Dear EU Leaders,

Ahead of the Energy Council on October 15 and European Council on 17 & 18 October and we would like to share the power sector's perspective on how to bolster European competitiveness while retaining investor confidence in the power sector – *the* key sector for clean transition.

Overall, we welcome the report by Mario Draghi and commend the comprehensive analysis of key elements that, in combination, will be needed to improve European competitiveness. In particular, it is positive that the report identifies accelerated electrification – meaning the use of electricity to power our homes, vehicles and industrial processes - along with a significant expansion of the electricity system as the way forward. This is consistent with REPowerEU when you, EU leaders, agreed that the best insurance against future energy supply shocks is increasing reliance on domestic and clean electricity. This is not an only a climate imperative, it is an acknowledgement of the geological realities of the EU.

At the same time, it is clear that bolstering energy-cost competitiveness of energy intensive industries while sustaining continued investments in the power sector will require a balanced and carefully crafted approach.

We call on EU leaders to deliberate around the following basic principles:

1. **The power sector and the industrial base must grow together**

While actions must be taken to ensure industry competitiveness, we also need to ensure that the power sector remains not only investible, but attractive to be able to tap into required private capital from financial markets.

Today, Europe is recovering from the energy crisis. Wholesale electricity prices are consolidating at significantly lower levels than in 2022-2023. On top of that, low capture rates and frequent instances of negative prices are becoming the new normal in the market as more renewables are added to the system. Reducing this volatility is beneficial for our sector and industrial consumers. It requires investments in flexibility in the power system (flexible generation, storage and demand response) and upsizing our power grids at transmission and distribution level.

2. **Electrification of demand must grow in tandem with supply**

As our industry is financing the growth of domestic electricity generation and grid infrastructure, we count on demand to grow in synchronicity. Electrifying consumption is a pragmatic way to distribute the costs more fairly and to improve security of supply for an economy and society that can prosper.

Yet today's reality looks strikingly different. Europe's energy consumption is only 23% electric, stagnating for the better part of the last decade. Since 2021, electricity consumption even decreased by 7.5%, a trend counter to our strategic goals.

3. **Be aware of the unwanted trade-offs in short-term measures**

Price relief for specific industrial users granted within the power market (by interventions on pricing or exemptions granted for the use of the system) will shift the cost burden onto other electricity consumers such as households and small businesses. This is not only an undesired social impact, but it has a negative multiplication effect over time on the uptake of heat pumps and electric mobility. Direct aid for industrial users that are exposed to international competition and based on a robust industrial policy are the better alternative.

It is crucial to avoid unintended effect on energy prices by distorting market dynamics, increasing system costs and ultimately eroding investor confidence at a time when their capital is crucially needed.

We therefore call for cautious deliberation over the report's recommendations. There is a thin line between incentives for industrials and disincentives for power sector investors.

The power sector stands ready to help strike the balance and to act on the recommendations that have the surest potential to strengthen our competitiveness in Europe.

Yours sincerely,

Leonhard Birnbaum
President

Kristian Ruby
Secretary General

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Annex

5 Elements that will bolster European competitiveness

1. Implementing the agreed electricity market design: The report confirms the internal energy market and its marginal pricing has reduced price variation across EU countries and delivered billions in cost savings to both household and businesses. With the recent reform of the electricity market, the focus should now be on implementation.
2. Developing long term contracts for industrials: PPAs and CfDs can reduce volatility from short-term markets and help transfer the benefits of renewable and clean energy to consumers and make power prices competitive. Incentivising PPAs will help consumers hedge excessive price volatility and should be prioritised in the next Commission mandate.
3. Focusing on needed investment in flexibility and transmission and distribution networks: There is an urgent need to address physical network bottlenecks, mitigate congestions, and ensure supply security across Member States. We must coordinate efforts to expand cross-border interconnections and improve domestic grid infrastructure.
4. Reducing taxes and levies to incentivise electrification: It is essential to reduce taxes and levies that disproportionately impact electricity prices, especially for industrial consumers. Today, electricity is taxed 1.4 times more than gas. Correcting this imbalance would incentivise the switch to electric decarbonised energy sources.
5. Streamlining permitting procedures for renewable energy and grid infrastructure: This includes enforcing an appropriate implementation of the recently agreed Renewable Energy Directive as well as further accelerating permitting for grids.

4 Elements that would negatively impact investor confidence in the power sector

1. Inframarginal price caps: The report acknowledges the negative effects of the inframarginal price cap during 2021-2023 but still suggests adopting **similar emergency measures in case of energy crises**. The power sector cautions against invoking a semi-permanent state of crisis with frequent interventions in the market as this will deter investors.
2. Extension of long-term contracts and support mechanisms to all renewable and nuclear assets: These measures could negatively affect investor confidence and effective dispatch. The critical value of hydro power, for instance, is that it dispatches on scarcity signals from the market. Politically forced long-term contracts risk turning it into a baseload resource with less system value.
3. Introducing banking-like regulation on energy players by removing the MiFID ancillary activity exemption: The report suggests significant regulatory changes to the energy trading environment. Energy markets are fundamentally distinct from financial markets because they serve the optimisation of physical assets. A removal of the ancillary activity exemption under Mifid would amplify the liquidity strains and affect the investment capacity of utilities. It would also lower the ability to hedge risks and thus could result in higher energy costs for consumers.
4. Predefined minor share of their publicly subsidised production through PPAs: A potential requirement to supply a predefined minor share of their publicly subsidised production through PPAs at 'production cost plus mark-up' to specific industries exposed to international competition" is concerning. This would not reflect other considerations that should be part of a PPA negotiation such as credit risk of off-takers, risk premiums to cover for long term risks and be disruptive for the market functioning.