

CABINET POTOČNIK				
Archives n° A				
19. 11. 2012				
Tc	MM			
Cc				



Paris, 6th November 2012
PrD-12/414

Dear Commissioner,

The EU power sector currently faces two crucial challenges: the modernization of an aging generation fleet and the transition towards a technology-neutral low-carbon economy, bearing in mind that both need to take place at least cost and to support the European industry. Although AREVA does not invest in power generation assets, the group – as a low-carbon technology provider – is in a privileged position to observe how its utility customers face such challenges.

For the last two decades, **utilities' cash flows available for self-financing have decreased, as well as utilities' ability to rely solely on their balance sheet (corporate finance).** Requirements to keep up with tightening carbon regulation, regulated assets disposal, ageing grids and consolidation of the European market have left even the largest utilities with limited capacity to lead more than one or two large projects at the same time (be it for large offshore wind farms, new nuclear power plants or Carbon Capture and Storage (CCS) projects).

While the business case for investments in low-carbon power generation technologies is clear (stable, predictable and low operating costs), **it increasingly depends on investors outside the power industry who are not used to dealing with the long term investment cycles – several decades – that distinguish it.** Investors still find themselves rather reluctant to engage in financing projects for several reasons, which require actions from policy makers, regulators and the industry.

Commissioner Janez Potocnik
European Commission
200 rue de la Loi
1000 Brussels
Belgium



1. **Regulatory certainty is required to provide visibility and enhance investors' confidence:** The liberalization of the electricity market aimed at market players taking their investment decisions on pure market terms. However, a stack of ad hoc tariff distortions have been progressively piling up in recent years (subsidies for renewables, capacity, grid development, electro-intensive industries, Combined Heat and Power, energy poverty...): they contribute to making energy prices less transparent and harm the overall efficiency of the EU energy policy as they keep changing regularly. Subsidies for renewables account for over €20bn each year across the EU— directly inflating the final electricity price – and are bound to increase sharply in the coming years. AREVA calls for a progressive removal of these market distortions (e.g. as renewables reach grids parity) and for a long-term regulatory framework based on robust carbon pricing.
2. **Environmental externalities are currently not adequately internalised:** The EU ETS system was implemented to direct investment towards low-carbon technologies. Due to initial free allowances and the current economic downturn, the ETS price has plunged to a level which no longer adequately reflects the full long-term cost of the carbon externalities. AREVA supports the Commission's proposal to bring scarcity in the EU ETS market as a short-term measure. This proposal should be followed by an early adoption of a post-2020 ETS extension to guarantee an adequate and predictable carbon price. For this purpose, AREVA supports an intermediary 2030 target expressed as a carbon emission reduction (-40%). A market-based approach may not fully succeed in steering utilities' investments towards low-carbon solutions: the implementation of a carbon tax or a carbon price floor may prove more effective at providing the appropriate level of visibility for such long-term investments to materialize.
3. **Current market arrangements need to evolve to foster investment in capital intensive generation technologies:** With an increasing share of low-carbon energy sources, the current wholesale market model based on short-run marginal cost pricing will increasingly lead to highly volatile and deflated electricity prices and lower load factors. This design fails to send the right price signals to stimulate investment in capital intensive low-carbon technologies as the required recovery of the initial capital investment becomes less secured. As mentioned in the "Energy roadmap 2050" communication earlier this year, "market arrangements need to be ready for the challenges decarbonisation will bring" and "all types of capacity (variable, baseload, flexible) should expect a reasonable return on investment". Having the possibility of using long-term Power Purchase Agreements would only seem consistent with the Commission's long-standing approval of support mechanisms to renewables power generation (such as feed-in-tariffs) - granted for decade-long periods - and would instate a level playing field between low-carbon technologies. AREVA calls for improved possibilities to use technology-neutral long-term contractual arrangements such as power-user investments (e.g. Mankala in Finland), Power Purchase Agreements (e.g. Exeltium in France) or more ambitious market reforms as currently discussed in the UK.



4. **Low-carbon technologies face limited track-record that calls for temporary measures:** Beyond the challenges faced by any other infrastructure mega projects, the limited track record for most low-carbon technologies (be it Generation 3 nuclear new build or less mature renewables such as offshore wind, solar CSP) increases the perceived financial risk in the construction phase. However, most of these risks will disappear once there is a flow of successful projects: innovation efforts should thus be sustained to materialise further costs reductions shortly. In the meantime, temporary public support to low-carbon technologies may be required to reduce the perceived risk of such projects and attract private investors. The European Commission and the European Investment Bank have been effective catalysts in the renewables sector (European Energy Recovery Program, direct loans, future project bonds...) and in the transport sector (Loan Guarantee Instrument for Trans-European Transport Network Projects); Euratom loans played a similar role in the 1980s. Credit guarantees should continue to be used as a catalyst to ease financing of low-carbon technologies.
5. **The tighter constraints on banks' liquidity need to be overcome:** Utilities face increasing capital scarcity to finance their projects, which are competing globally with other infrastructure sectors. The consequences of the financial crisis and the upcoming Basel III rules should not hinder long-term investments in the real economy.
6. **Global competition distortions issues need to be addressed:** non European governments – such as Russia, the United States, Japan and China – are currently dedicating credit lines to promote exports in low-carbon energy solutions. AREVA calls on the Commission to effectively address the distortion of competition linked to the financing of any infrastructure project in Europe.

In conclusion, **the best way for Europe to guarantee that the required investment in low-carbon power generation technologies is made in due time, at a competitive cost and in support of the European industry is to address the financing challenge**. It equally affects all types of low-carbon technologies – nuclear and less mature renewable energies – and as such calls for technology-neutral policy answers at European level.

I hope these views prove to be useful and look forward to meeting you.

Yours sincerely,



Luc Oursel
Chief Executive Officer