

ELECTRICITY: COSTS AND COMPETITIVENESS

- *Supply uncertainty and the high cost of electricity have become major obstacles to the competitiveness of Brazilian industry.*
- *Rising electricity costs in Brazil are a consequence of unsuccessful regulatory interventions, of the vulnerability of the energy matrix to adverse hydrological scenarios, and of the high charges applied to the sector, incentives and cross subsidies in the composition of electricity rates.*
- *In order to bring the cost of electricity down to competitive levels, it is necessary to ensure institutional stability and legal certainty in the electricity industry, as well as to reassess regulatory measures such as the duration of contracts and charges, incentives and subsidies.*

Electricity is one of the main inputs of Brazilian industry. Supply certainty and its cost are key determinants of the competitiveness of industry.

The Brazilian electrical system was once seen as one of the most efficient systems in the world. Large hydroelectric dams ensure the safety of the system and the low cost of electricity. This situation represented a comparative advantage for the Brazilian economy. Unfortunately, those days have passed.

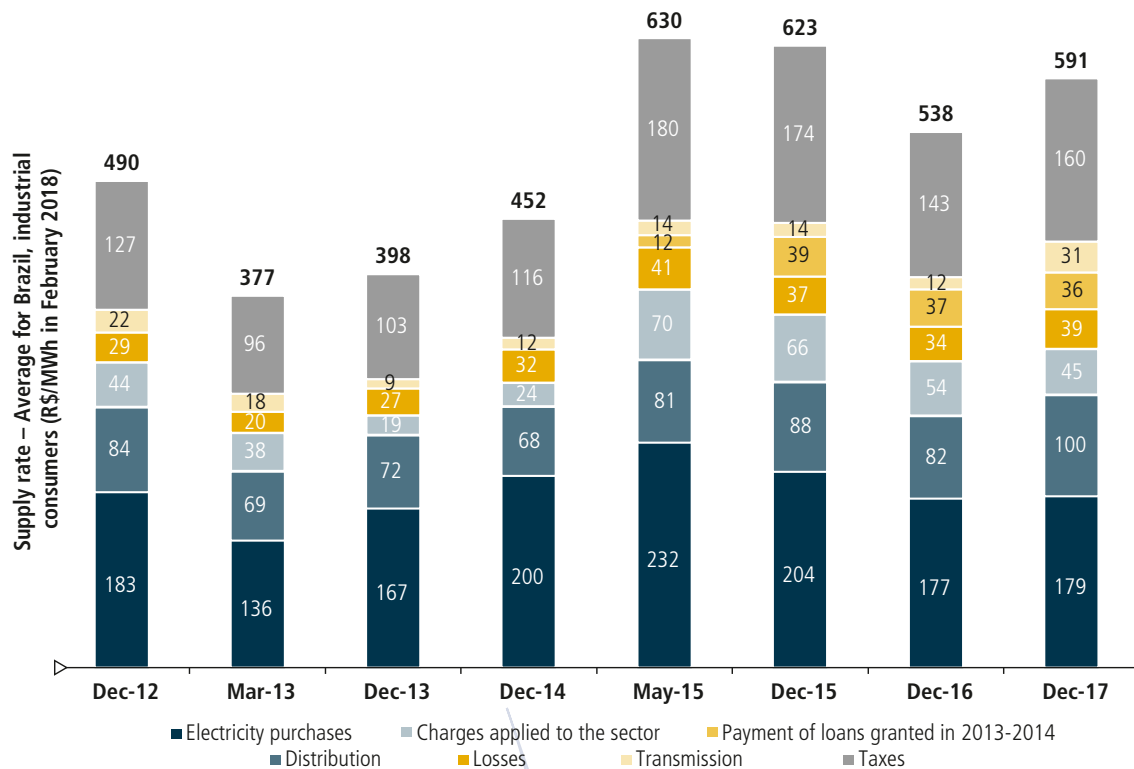
Constant government interventions coupled with high tax costs and charges applied to the sector and regulatory errors have turned the electricity rates paid by industry into some of the most expensive ones in the world. According to data from ANEEL, in the period from January 2013 to the end of 2017 the cost of electricity for industrial consumers, which buy energy directly from distributors, rose by 57% in real terms.

If nothing is done, the prospects will not be very encouraging. If the current regulatory and contractual conditions remain unchanged, expanding power generation and transmission will not lead to a sustainable reduction in the cost of electricity. It is also necessary to review the policy of charges and subsidies and reduce them. A positive development is that the last installments of sectoral financial liabilities will be paid between 2019 and 2020.

The main reasons of the high cost of energy in Brazil are the following ones:

- increase in energy contract prices;
- cost of liabilities arising from government interventions for regulating rates and prices;
- high cost of electricity rate subsidies;
- increased costs with the transmission system; and
- a heavy tax burden.

AVERAGE ELECTRICITY SUPPLY RATE FOR CAPTIVE INDUSTRIAL CONSUMERS IN BRAZIL (THE AMOUNTS WERE ADJUSTED BY THE EXPANDED CONSUMER PRICE INDEX (IPCA) FOR THE BASE DATE OF FEBRUARY 2018)



Source: PSR, based on data from ANEEL. Consumption and distribution revenue reports. Brasília, 2018 and ANEEL. Results of distribution rate processes. Brasília, 2018.

Main recommendations

- 1 Institutional stability should be promoted**, especially in what regards regulation related to price and rate formation.
- 2 The charges applied to the sector, as well as incentives and subsidies, should be reduced**, and the allocation of remaining costs should be improved.
- 3 The duration of electricity contracts should be reduced**, making it possible for consumers to enjoy price reductions derived from technological advancements.
- 4 The allocation of expansion costs between regulated and free consumers should be improved.**
- 5 The allocation of market risks to generators, who are best able to manage them, should be given priority.**
- 6 The agents operating in the infrastructure investment market should be diversified.**
- 7 The expansion of electricity generation and transmission should be jointly optimized.**

The full version of the document can be accessed through the QR code on the side or at: <http://www.cni.com.br/eleicoes2018/downloads/>. This summary is part of the series Proposals of Industry for the 2018 Elections comprising 43 documents. The series, which is based on the *2018-2022 Strategy Map for Industry* is a CNI contribution to the new federal administration and presents analyses and proposals of priorities to increase Brazil's competitiveness. Any part of this publication may be copied, provided that the source is acknowledged. Brasília-DF, July 2018.

