

Energy: international tensions and oil price increase electricity +6.5% and gas +8.2%

oil crude price rose by 57% in a year, driving up all energy commodity prices

Milan, 28 June 2018 – The international tensions and the consequent strong acceleration of oil prices, rose by 57% in one year¹ and by 9% in May alone, have heavily influenced energy prices in wholesale markets, with repercussions on prices to consumers of both the free market and the market with a reference price. These trends are reflected in the updating of *reference prices* for households and small consumers of the standard offer market for the third quarter of 2018. For the electricity sector, in order to mitigate the impact of the current economic situation, the Authority intervened by modulating the system's general charges, to reduce the increase in expenditure for both domestic and non-domestic consumers, with equal effects both on the market with a reference price and on the free market. As a consequence, from next 1 July, the expenditure on energy for the average household in the standard offer market² will record an increase of 6.5% for electricity and 8.2% for natural gas, in contrast to the hefty reduction (-8% for electricity and -5.7% for gas) in the second quarter of 2018. For gas, the impact on expenditure for domestic consumers is less significant given the very low consumption over the summer period.

As stated, the increase in electricity price would have been more consistent in the absence of the important 'shield' intervention put in place by the Authority through the system charges³, whose total value for 2018 is estimated at 14 billion Euro. In order to limit increases on consumers with immediate effect, the Authority has decided to partly reduce the weight of general charges on tariffs, by compensating them with the shield of its cash-holding. This measure will benefit all consumers in the same way, both in the standard offer market and the free market. It has been made possible by the budget consolidation policy implemented by the Regulator in the last 7 years, even if on the direction of a threefold increase in charges, which has made it possible to cover the 2011 financial deficit. The reduction in charges for the July-September 2018 quarter shall be reintegrated with future recovery interventions on the same consumers.

For electricity, the cost for the average household (including tax) in the rolling year⁴ (between 1 October 2017 and 30 September 2018) will be Euro 537, up 4.8% compared with the same twelve months last year (1 October 2016 – 30 September 2017), equal to an increase of about 24 Euro/year. In the same period, the average household's expenditure on the *gas bill* will be approximately Euro 1,050, up 2% on the same twelve months of the previous year (1 October 2016 – 30 September 2017), and equal to about 21 Euro/year.

¹ The Brent barrel, reference for Europe over the last 12 months, has gone from around 50 dollars/barrel in May 2017, to about 78 dollars in May 2018 (+57%).

² The average household has an average electricity consumption of 2,700 kWh per year and a maximum subscribed power of 3 kW; for gas, consumption is 1,400 cubic metres per year.

³ The general system charges, which are parafiscal, are required by the law to finance specific objectives of general interest (e.g., to support renewable source development, for subsidies to electric energy-intensive businesses, to support system research, social bonuses, etc.). These charges amount to about 25 % of the average domestic consumer's *bill*.

⁴ The rolling year means the year comprising the quarter covered in the update and the three preceding quarters, also taking into consideration the consumption associated with each quarter.

In May the wholesale price of electricity (PUN - National Single Price) recorded sharp increases compared to the same month in 2017 and June's preliminary year-end data shows a further rise; in the same period, significant increases were also recorded in numerous European power exchanges⁵. Furthermore, the indications coming from the forward markets, although with oscillations and recent signs of a slow-down in growth, seem to confirm an uptrend for the next July-September quarter. To this the following should be added: the seasonality effect, which in the third quarter sees electricity prices traditionally higher than in other quarters (in the last three years the prices were higher on average than 17%); wholesale prices of gas at the Virtual Trading Point (VTP) (the Italian wholesale market) in May were greater by about 30% compared to May of a year ago (with even more marked increases in the major European hubs, with the Dutch TTF price that same month increasing by 38% on an annual basis) and were expected to be also high in the next July-September quarter. High gas prices determined by geopolitical factors, but also by the high demand to fill the stockpiles for winter, and which are pushing electricity production prices upwards.

Electricity - In more detail, the increase in electricity for the average household would have led to a strong growth in the costs of supply, which would contribute by +12.5% to the variation of overall expenditure for the average consumer (already net of a slight decrease in dispatching costs, especially for the reduction of costs for the interruptible power plants). This increase was offset by the -6 % reduction of the system's general charges (an effect of the 'shield' intervention), determined by the -2.3% of the *A_{SOS}* component (the general charges for supporting renewable energy) and by the -3.7% of the *A_{RIM}* component (to cover other charges). In particular, all the rates of the *A_{RIM}* component are reset for a quarter for all customers, both domestic and non-domestic, whereas the variable rates of the *A_{SOS}* component are only reduced for domestic customers. This is how we get to the final +6.5% for the average domestic consumer's overall spending.

Natural Gas - In more detail, the increase for gas is determined mainly by the strong growth in the *C_{MEM}* component relative to the costs of supply, +8.3% on expenditure for the average consumer, reflecting the expected increase of wholesale prices in forward markets in Italy and in Europe. Even the *Q_t* component relative to the transport service grew slightly (+0.4% on the average customer's expenditure), due to the increase in the charges to cover the transport from the VTP to the network's redelivery point for the charges resulting from the new gas settlement rules. On the other hand, a slight decline (-0.5%) was recorded for the UG3 component covering the arrears for last resort services. Thus we come to the overall +8.2% in expenditure for the average consumer, whose impact is less significant in view of the very low consumption during the summer period.

The quarterly update in detail

Aggregations and graphs in line with new elements introduced by 'Bill 2.0'⁶

⁵ Two digit increases in prices were recorded for electricity in May, even by the power exchanges of Spain (+28.7% on a cyclical basis and +16.6% on a trend basis), Belgium (+17.8% on a cyclical basis and 19.6% on a trend basis) and the Netherlands (+18.4% on a cyclical basis and +34.2% on a trend basis), while in Germany and the United Kingdom the increments were more contained in comparison with the previous month (around +4.5%) but significant compared to a year ago (+10.1% and +26.0% respectively). In the first half of June, with respect to the average value of May, the upward trend has undergone an acceleration in Germany (+37.5%), France (+28.7%) and Belgium (+24.2%).

⁶In detail, the Bill 2.0 provides for the simplification of the content and terms used in the summary bill sent to everyone, which is essential to understanding the final expenditure. The first page of the bill also shows the average unit cost per kilowatt-hour/standard cubic meter, as a ratio between total expenditure and billed consumption. Anyone wishing to get more information on the various items can ask their provider for details, i.e., additional pages containing a full description of the components making up the overall expenditure. The full details will always be provided when responding to a complaint. The 'System charges expenditure', an item shown as part of the grid

Electricity - From 1 July 2018, the average consumer price for electricity will be 20.22 Euro cents per kilowatt hour, including taxes, broken down as follows⁷:

Energy material charges:

- 8.81 Euro cents (43.57% of the total bill) for energy supply costs;
- 1.67 Euro cents (8.26%) for retail marketing.

Transportation and meter management charges:

- 3.87 Euro cents (19.14%) for distribution, metering, transport, transmission and distribution equalization and quality.

System charges:

- 3.22 Euro cents (15.92%) for general system charges, set by law.

Taxes:

- 2.65 Euro cents (13.11%) for taxes, which include VAT and excise duties.

In the 3rd quarter of 2018, system charges are divided as follows:

In implementation of Decree-Law 210/15 and in view of the decision of the European Commission concerning the compatibility of the measures benefitting electric energy-intensive companies with the European rules on State Aid (Decision C (2017) 3406), the Authority has updated the general structure of the groupings and of the components of the electricity system general charges in its Resolution 481/2017.

From 1 January 2018 it has thus provided that the rates of general charges relating to the components A2, A3, A4, A5, As, MCT, UC4, UC7 and the additional components to be applied to all types of contract will be separated into the following groupings: 'General charges related to the support of renewable energy and cogeneration' (ASOS), which includes all costs covered by the A3tariff component up until 31 December 2017, with the exclusion of the cost items related to production attributable to non-biodegradable waste; 'Remaining general charges' (A_{RI}M).

Considering the zeroing of the A_{RI}M component, in the third quarter of 2018 the A_{SOS} component amounts to 100% of general charges, and is split between the following two items:

- 78.74% for the incentives for renewable energy sources and CIP 6/92 cogeneration (share of old A3 component);
- 21.26% for the aids to the electric energy-intensive companies (old 'Ae' component).

It should be remembered that the A_{RI}M component is split between the following items:

- promotion of energy efficiency (UC7 component);
- nuclear safety and local compensation (A2 and MCT components), including the €135 million per year for the State Budget;
- system research support (A5 component);

services up to now, is also shown explicitly and clarified in the event of any recalculations, i.e., adjustments, which are in turn highlighted in a dedicated box.

⁷Starting 1 January 2016, the Resolution 200/2015/R/COM of 30 April 2015, – Bill 2.0 – provides a different aggregation of the single invoice components billed to the consumers; specifically, the items that were included in *Sale services* are merged as they are with the item *Energy Material Charges*, whereas the items that were included in *Grid services* are divided in two separate aggregations, which are *Transportation and meter management charges* (distribution, metering, transport, transmission and distribution equalization and quality) and *System charges*.

- compensations for minor electricity enterprises (UC4 component);
- special tariff schemes for the universal rail and goods service (A4 component);
- electricity bonus (As component);
- incentives for energy production from non-biodegradable waste (share of old A3 component).

Natural gas - In detail, from 1 July 2016, the *gas reference price* for the average consumer will be 78.28 Euro cents per cubic metre, including taxes, divided as follows⁸:

Natural gas material costs:

- 28.39 Euro cents (36.27% of the bill total) for the natural gas supply and related activities;
- 5.08 Euro cents (6.49%) for retail sale.

Transport and meter management charges:

- 13.40 Euro cents (17.12%) for the distribution, metering, transport, transmission and distribution equalization and quality control services.

System charges:

- 2.21 Euro cents (2.82%) for general system charges, established by law.

Taxes:

- 29.20 Euro cents (37.30%) for taxes including excise duties (19.53%), regional surtax (2.59%) and VAT (15.18%).

All resolutions are available on the ARERA website at www.arera.it.

⁸ Starting 1 January 2016, Resolution 200/2015/R/COM of 30 April 2015 – Bill 2.0 – provides a different aggregation of the single invoice components billed to the consumers; specifically, the items that were included in *Sale services* are merged as they are with the item *Natural Gas Material Charges*, whereas the items that were included in *Network services* are divided in two separate aggregations, which are *Transportation and meter management charges* (distribution, metering, transport, distribution equalization and quality) and *System charges* (equalization of sales and marketing, last resort service arrears and energy saving and renewable energy development interventions).