

#### **Box 4**

##### **Recent developments in network industries**

Regulatory reforms in European network industries are widely considered as being beneficial to consumers in terms of entailing lower prices.<sup>1</sup> This box reviews the recent progress made with regulatory reforms in the telecommunications, electricity and gas sectors and describes price developments in these sectors relative to overall HICP developments. Telecommunications, electricity and gas taken together account for almost 6% of the overall euro area HICP.

Regulatory reforms in the telecommunications sector have continued to exert a downward influence on price developments, albeit significantly less than in the initial years following market liberalisation. Increased competition is required, especially in the energy sector.

##### **Recent progress in regulatory reforms**

The regulatory reform process is most advanced in the **telecommunications sector**, although effective competition in a number of countries and market segments remains rather limited, in particular on account of

*1 See, for example, European Central Bank, "Price effects of regulatory reform in selected network industries", March 2001.*

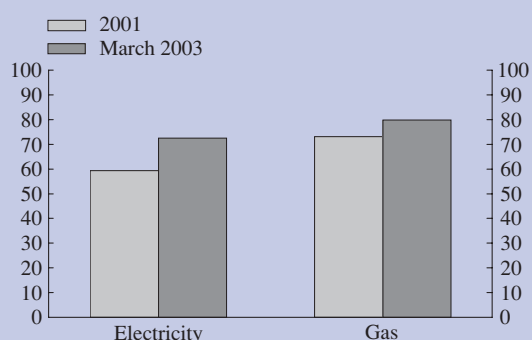
the fact that incumbent operators still retain a significant market share. The mobile phone market share of the subsidiaries of incumbent fixed operators was above 40% in each euro area country in 2002, the most recent year for which information is available.<sup>2</sup> The market share of the incumbents in fixed telecommunications in each euro area country was even larger: generally above 80% for local calls and between 60% and 80% for long-distance and international calls.

In the **electricity market**, several euro area countries have extended the degree of market opening since 2001. The chart below shows the percentage share of the euro area electricity market open to competition by March 2003 and the progress achieved since 2001. More than 70% of the euro area electricity market is now formally open to competition, even if significant differences among euro area countries still exist, with France and Greece having the lowest degree of electricity market opening (slightly above 30%). Despite progress in the formal opening of the electricity market in some countries, competition often remains limited, mainly on account of the position of dominant incumbents and weak regulatory authorities.

The **gas market** has opened up further since 2001. Close to 80% of the euro area gas market is now formally open to competition, but effective competition still seems relatively limited and clearly lower than in the electricity sector. The main obstacles to competition are disparities in network access tariffs across countries and regions, the concentration of gas production and import in a few companies and the slow development of gas trading hubs, preventing new entrants from buying wholesale gas.

All in all, regulatory reforms in network industries progressed further in 2002 and in 2003, albeit with differences across sectors and countries. In November 2002 the EU Transport, Telecommunications and Energy Council set a timetable for full energy market opening, with a deadline of 1 July 2004 for non-household users and 1 July 2007 for household users. This agreement represents an important step forward in the liberalisation of energy markets.

**Percentage share of euro area energy market open for competition**



Sources: European Commission and ECB calculations. The ECB calculation of the euro area market shares is based on electricity and gas demand weights in 2001 and 2002 respectively. For the gas market, data for Greece, Portugal and Finland are missing.

### Price developments in network industries

Following the gradual introduction of regulatory reforms in the **telecommunications sector**, prices in the euro area continued to decline in 2002 and in 2003, albeit at a considerably slower pace than during the period 2000-01 (see the table below). In 2002 and in the period from January to September 2003, the HICP sub-index for telecommunications services continued to contribute negatively to overall HICP inflation, albeit only marginally. Since 2000, however, the cumulative downward effect of the HICP sub-index for telecommunications on total HICP inflation has been quite large and amounts to 0.33 percentage point.

The HICP sub-index for **electricity** for the euro area as a whole rose by 2.8% during the period from January to September 2003, which was higher than overall HICP inflation. However, the average increase over the period 2000-02 was lower than the one for overall HICP. Electricity prices continued to be strongly affected by factors that are independent of the chosen regulatory regime, such as the mix of primary energy sources, fuel prices and country-specific effects (e.g. changes in indirect taxation). Moreover, price developments over recent

<sup>2</sup> The source of market shares data in the telecommunications sector is Eurostat.

### Contribution of telecommunications, electricity and gas prices to the overall euro area HICP

	Annual percentage change				Contribution to HICP (change in percentage points)				
	2000	2001	2002	Jan.-Sep. 2003	2000	2001	2002	Jan.-Sep. 2003	2000-Sep. 2003
Total HICP	2.1	2.3	2.3	2.1					
Telecoms	-8.2	-4.9	-0.6	-0.5	-0.20	-0.11	-0.01	-0.01	-0.33
Electricity	-1.1	2.0	1.8	2.8	-0.02	0.04	0.04	0.06	0.11
Gas	11.6	14.7	-2.3	4.4	0.15	0.21	-0.03	0.06	0.38

Sources: Eurostat and ECB calculations.

years are more likely to have reflected pre-emptive pricing policies by incumbents and price setting by the regulators than the impact of the limited effective competition in the electricity sector. Increased competition will be essential to ensure favourable price developments.

Developments in **gas prices** only partly reflect changes in the level of competition, while prices are largely affected by the underlying evolution of world market energy prices and the exchange rate of the euro. Gas prices in the euro area, as measured by the HICP sub-index, decreased by 2.3% in 2002, with the result that the HICP sub-index for gas contributed negatively to overall HICP inflation. This was reversed in 2003, and the contribution of gas to overall HICP inflation in the euro area during the period from January to September 2003 was 0.06 percentage point. As with the electricity sector, further regulatory reforms are needed to allow more incumbent rents to be distributed to consumers.

Price level dispersion across euro area countries declined slightly last year for national and international telephone calls, gas prices and households' electricity prices. However, significant differences in price developments across countries and types of service still exist in all network industries and reflect, among other things, an uneven progress in the implementation of regulatory reforms and the different regime of indirect taxation across countries.