POSITION PAPER
POWER AND ENERGY SUB-GROUP

Prepared by
Power and Energy Sub-Working Group

The Government has done a good job in ensuring sufficient energy through 2014/15, however the members of the Working Group and their respective Chambers, Business Associations and member are concerned about the uncertain outlook of power supply especially information put out by MOIT on May 15th about expected shortages in the south of Vietnam in-line with international agreements with Cambodia and Lao. In early 2015 VBF facilitated a study with IISD/MPI/ United Kingdom Embassy and UNDP on understanding the needs and concerns of foreign businesses with regard to energy supply and reliability and how energy prices are going to drive their investment decision in Viet Nam. We appreciate comments by MOIT.

Below are key conclusions from the main report sent to MOIT and MPI.

1. **Viet Nam's ability to attract FDI is NOT based on low energy prices.** Stakeholder analysis and survey results indicate that firms do not typically invest in Viet Nam as a result of the fact that energy prices have been historically low. In fact, firms ranked the state of power prices to be **the least** important factor of ten factors in their decision to invest in Vietnam. Much more important in their investment decisions were other drivers such as the cost and availability of skilled labor, domestic market condition and Government development policy. When asked to rank the importance of energy prices as a driver for investment decisions (on an increasing scale of 1-10), 72 per cent of firms indicated a score of 5 or less.

2. **On the whole, foreign investors are not seriously concerned about the prospect of gradually higher power prices.** This is likely partly to do with the fact that firms spend relatively little on electricity. The study found that 90 per cent of foreign firms across all sectors spend less than 10 per cent of total operating costs on electricity, with 60 per cent of firms spending less than 5 per cent.The majority of firms indicated that they would be willing to bear sustained nominal annual power prices increases of 15 per cent or more before reconsidering future investment, and more than 65 per cent of firms were willing to bear sustained price rises of more than 10 per cent per annum. Indeed, the majority of firms that had made recent investments had already incorporated higher power prices (with an average increase of 10 per cent) into their investment decisions. Sustained annual industrial electricity tariff increases of 15 per cent would contribute significantly towards the achievement of cost recovery over time.

   This message was again reiterated in stakeholder analysis. Firms made it clear that they understand that EVN continues to run at a large loss, that electricity costs remain the lowest in the region, that generation capacity addition and power supply have become increasing unreliable and that there is therefore a need to raise power prices to cover costs and encourage energy sector investment, both from EVN and the private-sector.

3. **Based on these findings, the Vietnamese Government should be more ambitious in raising the price that large industrial consumers pay for power.** Firstly, firms have clearly indicated that energy prices are not a key driver of foreign investment in Viet Nam. Secondly, as presented throughout this report, firms have also shown some willingness to accept higher power prices over time as a key means of enhancing the functioning of Vietnam's electricity sector. This provides space for the Vietnamese Government to be more determined in moving towards charging large industrial users

the full cost of power, without being concerned that by doing so they will cause a significant adverse investment response from multinationals.

4. **Firms are concerned by the inadequacy of power supply and the prospects for diminishing supply reliability, more so than by the prospect of higher power prices.** Sixty-five per cent of firms indicated that they were either rather unsatisfied or not satisfied at all with power infrastructure and supply. Two-thirds of firms who disclosed information said that they used back-up generation either 'sometimes' or 'often'. Further, a large majority (73 per cent) of firms said that the unreliability of power supply was more damaging to Vietnamese investment competitiveness than the prospect of higher power prices over time. Given the linkages between low power prices and inadequate investment in supply capacity, this seems to suggest a willingness to accept higher prices in exchange for much improved electricity system functioning. Indeed, the survey found that even 60 per cent of energy intensive industry and other heavy manufacturing firms were willing to accept an immediate nominal increase in power prices by 20 per cent in exchange for uninterrupted power supply.

   Ensuring adequate power supply should therefore be *the* key priority of Vietnamese energy policy, along with a long-term movement towards greener modes of electricity generation. As such, a key focus of the crucial revisions to PDP7 should be the identification, design and ultimate implementation of new mechanisms and incentives that can enhance investment and supply reliability in power markets. Indeed, enhancing electricity sector investment will likely only take place with higher tariffs for grid electricity (to increasingly provide investment capital to EVN), higher PPAs to encourage new private sector BOTs, and the development of a legal framework for investment that makes the latter – especially for renewable generation – possible.

5. **There is significant space (and necessity) for private-sector solutions to Viet Nam's power supply needs.** Given both the current inefficiency of EVN and the difficulty of EVN in allocating investment capital, private sector investment will likely need to play an increasingly important role in securing adequate electricity supply in Viet Nam over time. Renewable generation, in particular, is well-placed to meet growing energy needs due to its scalability over short time frames, with wind power being particularly promising given the extensive pipeline (4.4 GW) of registered projects and existing (although currently inadequate) Government support policy. Again, however, this will require higher grid tariffs, higher PPAs to encourage new private sector investments, and a new enabling legal framework for investment. Working towards these three outcomes should be a priority for Government, and should be addressed in the important ongoing process to revise PDP7.

6. **Despite the need for greater ambition in increasing power prices to industrial users, a gradualist approach to price rises should be pursued.** While firms are on the whole willing to accept higher power prices over time, there are limits as to what firms can realistically absorb in the short-term in terms of higher power costs. Survey results suggest that only a few firms are willing to accept nominal power price increases much above 20 per cent per annum. While higher power prices are necessary, the Vietnamese Government should define and implement a gradual schedule for nominal industrial power tariff appreciation of 15-20 per cent per annum (with scope for larger increases depending on inflation rates) over three to four years. This would help to significantly address the issues associated with currently low power prices, while giving firms the certainty to plan accordingly and avoiding potentially damaging and destabilizing power price spikes.

The Power and Energy Sub Working Group have a continued relevance for cooperation and meetings with Ministry of Industry and Trade

- Renewable energy (RE) is best positioned to support Vietnam's energy needs in the near future due to its scalability during a short time frame. We look forwarded to receiving MOIT proposed updated "Feed In Tariffs for the Standard Power Purchase Agreement for Solar, Biomass plants and waste to energy", when they are ready. In order to bolster RE, the Working Group supports the creation of an attractive investment environment for these sectors. As such, the Group backs the recommendations put forth by MOIT consultants, which call for an increase in the FIT level for wind energy and simplification of application process.
- The working group agrees to set-up additional meetings with MOIT on the Direct Power Purchase Agreement option between electricity end users and independent Vietnamese power producers. The structure does not involve any physical transmission line between the two parties, meaning that the electricity will flow through the existing national grid currently used to transport electricity from the wind farm to the end user. In this model, the IPP and the energy users will negotiate an electricity price for a long term PPA and subsequently pay a wheeling fee to EVN for transmission, distribution and management of the electricity. The interest of implementing this model is high from FDI buyers of energy in Vietnam, developers and providers of technology, as well as banks to finance.
- The working group looks forward to receive the updated National Power Plan 7, for commenting on as mention by MOIT on 15 May, 2014
- EVN continues to run at a loss and electricity costs remain the lowest in the region. This limits both direct investments in grid infrastructure and energy efficiency efforts by customers. It is suggested to continue MOIT adjustment of energy tariffs for a sustainable power sector development in Vietnam as MOIT sees necessary. Important for FDI is for MOIT to share a road map of Retail Power Pricing to 2020 with a vision to 2030. This road map should come from the final authority. This will enable EVN in restructuring and becoming more profitable, open access to private investment both domestically and internationally, and will stimulate greater energy efficiency efforts from end use customers. We support the use of donor funds to off-set Government guarantees as Government reaches it limits in the coming year.
- EVN Rescue plan has been updated with EVN to be published in 2 months; VBF looks forwarded to get a copy. We understand from World Bank that the 10 years roadmap of reforms that EVN should take to meet certain financial indicators, standards. But as above a road map must come from the final authority.
- The Power and Energy Working Group emphasizes that the proposed strategy to support Vietnam's successful exploitation of natural resources for stable energy supply goes in line with the expected realization of Free Trade Agreements and to strengthen the private sector and SMEs to take advantage of upcoming FTAs. The expected boost in Vietnam's GDP and economic development, which is expected as a result Free Trade Agreements, will be founded on a strong power supply.
- Lastly the working group will work more to provide information on the planned increased coal policy over natural resources. To release the scale up of coal will require a major increase in infrastructure as existing infrastructure is handling an estimated 2.1 million tons and by 2020 we will need to import 38 million tons. Not clear who pays for needed infrastructure for coal import.