Getting Prices Right: Philippine energy policy should be guided by the country's climate vulnerability

Preliminary review of FILIPINO 2040 Energy: Power Security and Competitiveness

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We commend the EPDP for this initiative, as access to stable and secure power supply at affordable prices is key to the welfare of the Filipino people. The take-or-pay contracts forced on the government by the power crisis of the late 80's up to the early 90's have saddled us with stranded costs that we are paying up to now[1]. The mistakes of the past should not be repeated. We must not allow future generations to suffer from similar burdens resulting from poor policy.

ICSC is in full agreement with the authors' guiding principle of getting electricity prices right to ensure that government policies help to maximize social welfare. We in the NGO community have always strived to learn from and be guided by the academe, especially in regard to climate change theory and policy.

Welfare and Pricing

Let us address social welfare maximization first. The paper cites the price of electricity as an indicator of welfare. This is confusing because internalizing costs of greenhouse gas (GHG) emissions from electricity generation could really lead to higher electricity prices while, at the same time, increasing environmentally adjusted measures of welfare.

The paper attempts to incorporate the global warming externality (and local environmental effects) of electricity generation by putting a price on carbon. However, the carbon price was downscaled by the share of Philippine GDP in the world economy to capture only estimated effects on the country. We do not agree with this downscaling as explained below, but this specific method aggravates the ill effects because it ignores scientific findings that the Philippines suffers disproportionately more from global warming than its GDP share would indicate. The authors use a paper by Grayer and Viscusi (2014) that basically argues that EPA policies under the Obama administration encompass benefits of GHG reductions that accrued to citizens outside the United States, such that energy efficiency measures were overprovided. Thus, to maximize welfare for the US, these benefits should be excluded from any analysis. From the point of view of the citizens of the countries that suffer from such a method, this is clearly unacceptable.

1 https://pesd.fsi.stanford.edu/sites/default/files/PhilippinesIPP.pdf

Let's leave aside for the moment that the Philippines is among the worst victims of climate change induced by the historical cumulative emissions of the developed countries -- an injustice that certainly needs to be corrected. However, to downscale benefits of GHG reductions to only those that benefit Filipinos, as the Grayer and Viscusi method implies, means that it is alright for American and other citizens to make decisions that impinge on our welfare. If every country makes decisions this way, there can never be a solution to global warming. This lesson has, in many ways, affected the negotiating positions that have led to the historic Paris Agreement. Even after the surprise victory of Trump, responsible governments in Europe, and China have not balked.

The classic problem of free-riding with respect to the provision of public goods, which is the basic nature of GHG reduction, with benefits that are non-rival and non-excludable, does not yield to learning under repetitive games. The only rational recourse is cooperation, not free-riding. Climate change risks have to be dealt with now. This is why ICSC has fully supported the Paris Agreement and has been a key player in the Climate Vulnerable Forum (CVF). If we don't cooperate, it will be to our peril.

Competition and the Regulatory Regime

We laud the authors for their attention to the regulatory regime that is required for electricity end-users to face the right prices. This is tricky business and it will be some time before the regulators get it right. To cite just one fundamental difficulty, how can the Energy Regulatory Commission compare bids for baseload supply from thermal generation versus renewable energy with storage? The former have always been vetted based on capital recovery costs regardless of actual degree of utilization, and current fuel prices - with price volatility, spikes, and trend increases borne by ratepayers whereas the latter offer a levelized cost.

We also fully understand the concern by the authors of the potential effects of power sector policy on the competitiveness of Philippine industry and exports, but argue that long-term competitiveness rests also on getting input prices right. In a separate comment, we will focus on renewable energy price trends and their radical disruption of the regulatory regime, and potential stranded coal generation costs that may yet again be passed on to ratepayers, and offer ways forward. There are assumptions and approaches currently in the paper that require urgent attention, as it may defeat EPDP's goals, which as we said above we share.

We encourage the authors to take a look at the Energy Policy Review Inception Report of the Climate Change Commission. The report was a collaborative effort involving different agencies.

DoE Policy Now

The paper presents scenarios based on policy regimes and further distinguished by high and low economic growth projections, with conclusions that seemingly favor more coal generation. With the many limitations and caveats made by the authors themselves, we are inclined to view these as distractions from "getting prices right." Moreover, we are deeply concerned that this exercise has influenced the thinking of the DoE with renewable energy in its immediate policy agenda, especially the feed-in-tariff reform through auctions that we support. Over the past decades, the repeated policy failures to set a level playing field to get prices right have resulted to more misses than hits.

We agree with the authors that any arbitrary fuel-mix target is the wrong way to go. But getting prices right will take some time. We encourage the authors to look at more scenarios incorporating economic and technological trends, as well as the experience of other countries, to better ascertain optimal power outcomes.