Republic of Namibia

STATEMENT

PRESENTED BY HON CALLE SCHLETTWEIN, MINISTER OF TRADE AND INDUSTRY,

DURING THE NCCI NAMIBIAN ENERGY POLICY FORUM

AT THE

HILTON HOTEL, WINDHOEK

13 NOVEMBER 2014

Mr Tarah Shaanika, NCCI CEO and Master of Ceremonies;

Hon Isak Katali, Minister of Mines and Energy;

Mr Paulinus Shilamba, CEO of NAMPOWER;

Representative of the ECB;

Representatives of Business and Industry;

The NCCI Energy Working Group;

Members of the Media;

Ladies and Gentlemen.

I want to congratulate the NCCI for having constituted an energy working group and for having organised this very important Namibian Energy Policy Forum. I am also very grateful that my Ministry has been invited. I believe that dialogue between all stakeholders offers the best chance to solve difficult and complex issues and the current energy situation in the country is indeed such a challenge.

Energy security, alongside other enablers such as potable water, transport, telecom, Internet connectivity, and land availability, has a very important profile under the NDP4 goals. This is so, because all these enablers are prerequisites for bringing about accelerated economic growth, be it through value addition activities in manufacturing, agricultural production, tourism, transport, housing and sanitation, or any other economic activity, which are identified as the priority sectors for growth in NDP4. Security of supplies, cost and efficiency in the provision of services are key considerations investors take into account when deciding where and whether to set up business in a new locality. These are some of the challenges that need to be addressed.

Along with the general growth of the Namibian economy and the expansion of energy-intensive mining and manufacturing industries, country's energy consumption has been continuously increasing. It has been projected that the current peak demand will double to 1100MW by 2031. Ensuring a reliable supply of energy is of paramount importance for the general development of the country, but more so for the attainment of its industrialisation ambitions. Namibia is currently heavily reliant on imported energy (40-80%). The country is operating well below its installed generation capacity.

Under the NDP4, Namibia is aiming to expand its energy production from around 400MW to 750MW by 2017 to meet the spiralling domestic demand and become a net exporter.

Access to electricity remains an important issue, and given the size of the country, particularly so for rural areas. According to recent the estimates of the International Energy Agency, overall electrification rate stands at 34% (in rural locations at around 15%) which is slightly above Sub-Saharan African average, but well below the average across developing countries, Latin America and even Africa as a whole. In their annual report, NamPower has reiterated on its commitment to rural electrification, having increased the budget to N$20million in FY 2013 and initiated 17 projects.

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However, the central challenge is the affordability of energy, which poses a tremendous constraint on the Namibian economy. Without affordable and reliable supply of energy, it is a daunting task to attract investment particularly into the manufacturing, promote business activity, including start-ups and SMEs, and eradicate poverty and create employment especially in remote rural locations.

It is a well-known fact that Namibia has experienced a continuous growth in electricity prices over last years. A study on electricity tariffs conducted by the Namibia Manufacturers Association in 2012 concluded that since 1995 the bulk electricity tariffs in Namibia saw a five-fold increase. According to the Electricity Control Board estimates, over the last seven years, the average retail price of electricity has more than doubled. The general trend over time features a gradual annual growth, with steep hikes, however, taking place since 2009/10 driven by persistent general electricity shortages in the region.

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As a key input in many production processes, electricity and its prices, no doubt, matter for the general competitiveness of the Namibian economy, as besides the purchasing power and disposable income of households, they affect the production costs of industries and services. As a result, the high costs of electricity in Namibia have put a significant burden on all customer groups, but particularly the productive sector – commercial and industrial consumers, which are responsible for driving the economic growth of the whole country.

Therefore, as the Minister of Trade and Industry, I am highly concerned about the impact of high electricity costs on the productive sector of the economy, and particularly the manufacturing. Let me add here that it is our observation that most of the other enablers move on similar trajectories increasing the risk of spiralling Namibia's

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Put into context, Namibia's position relative to the SADC region is uncompetitive, as the country exhibits average electricity tariffs above the majority of the region, and based on the data available, second highest <u>industrial</u> tariff levels after Mauritius.

Namibia also continues to have significantly higher electricity prices than in region's largest economy South Africa. Despite a sharp decrease in electricity price differential from 70% in 2007, national residential tariffs in 2012 were still on average by 25% higher than in South Africa.

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A similar picture emerges when we look at tariff levels amongst industrialised developed nations. Namibia's average industrial tariff level is significantly above that of the European Union, Norway, the United States, being comparable only to Germany. The latter, however, has already announced its efforts to bring tariffs to a more competitive level. Germany recognises the paramount importance of electricity costs for the manufacturing sector of the economy.

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However, the future does not seem to bring relief to electricity users. NamPower has announced a minimum of 15% annual increase in costs for next years. This puts Namibia on a dangerous long-term trajectory of ever increasing electricity costs, with end user prices projected by the Electricity Control Board to already double within ten years. This, however, will happen in less than ten years if their low-income household subsidy model is approved. The proposed electricity support mechanism will yield a minimum 3% increase in electricity prices for cross-subsidizers on top of NamPower's projected hikes. As the result, Namibia's potential to industrialize will surely be eroded and competitiveness will be further reduced, not to mention the escalation of the costs of living.

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Potential effects of such tariff escalation are extremely detrimental for the productive sectors and thus the economy as a whole. International empirical evidence indicates that industrial customers tend to be more sensitive on average than residential customers to price increases.

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Manufacturers can significantly reduce their demand for electricity when the price increases by:

- Reducing overall production output;
- Switching from producing high to lower energy intensive goods;

- Opting to import instead of producing energy intensive goods;
- Exiting the public network switching to private generators.

This all goes against the national objective to industrialize and move away from the dependency on primary resource exports and imports of manufactured goods.

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The principal reason for these cost escalations is the model of electricity generation and distribution that we currently follow, namely that Government through Nampower develops, owns, operates and pays for all (thus far) infrastructure. This model is in my view only appropriate if there is no interest or capacity in the private sector to invest in electricity generation. That is most definitely not the case; whenever I have interacted with the private sector in Europe, Asia or North America over the past two years, investment interest in the energy sector is by far higher than in any other sector. I trust that State-driven electricity generation and distribution should thus only be considered together with the private investment appetite in the sector. Our inclination so far not to harness the capacity of the private sector to invest in electricity as a consequence means that our Government has to commit to enormous resource allocations and incur debt, which in turn threatens to undermine our macroeconomic stability.

I believe that procuring from Independent Power Producers through Power Purchase Agreements may need to be given a greater role in obtaining energy security for Namibia, provided that such power purchase agreements do not require government to cover for any risk it has no control over, there is not regulation freeze, performance guarantees by IPPs and NAMPOWER are included.

It is important to note that there is no requirement for any upfront capitalization by Government or Nampower for such procurements. The procurement process for such projects would nevertheless have to be very carefully managed, and the purchase or off take price for electricity should <u>not</u> be determined on the basis of the current electricity generation, distribution or retail prices in Namibia (which will lock us into a spiraling tariff cycle in the long term), but on the production and financing costs of each project proposed through competitive bidding. These costs will differ greatly from case to case and will vary according to technology used, fuel source, and the financial engineering of each project etc.

The criteria for such competitive bidding, amongst others, will be the employment creation, reduced tariff levels, higher generation efficiency, skill and technology transfer and local sourcing requirements. It is only through this approach that we would be able to increase competition in the domestic energy sector and reduce the current high cost of electricity for consumers, businesses and the industry.

I thank you for listening and look forward to partaking in this important discussion.