

## CHILE

# Time of crisis for energy transition

**Calls for constitutional reform, political infighting and the COVID-19 pandemic threaten Chile's energy transition programme, reports Maria Kielmas.**

Chile is facing its greatest political crisis of recent times, coupled with political uncertainties emerging from discussions on eventual constitutional change. These were the comments of Energy Minister Juan Carlos Jobet speaking at a June 2020 virtual meeting of the renewable energies grouping, Asociación Chilena de Energías Renovables y Almacenamiento (ACERA), on what should have been its annual dinner.

An energy strategy first established under the second presidency of Michelle Bachelet (2014–2018) and upheld by President Sebastián Piñera, also in his second term, committed Chile to a minimum 70% renewables share in energy production and a national carbon tax by 2050.

With limited conventional energy resources of its own, Chile imports all its oil, refined products, gas and most of its coal needs. The country is vulnerable to external energy price and political shocks – notably in 2008 when Argentina unilaterally cut off gas supplies. So, development and expansion of the country's ample resources for solar, wind and geothermal power supplies, as well as conventional hydropower, made sense from an energy security as well as environmental perspective. The plan to substitute coal, which makes up 40% of Chile's power generation capacity, with renewables resulted in the country being lauded internationally as a leader in sustainable development and decarbonisation.

## Hidden costs

However, the costs of this energy transition in terms of investment, end-user tariffs and potential unemployment did not come into public focus until October 2019. A 4% fare rise on the Santiago metro and a 9% rise in electricity

prices due to a new carbon tax triggered an explosion of social unrest and calls for changes to the 1980 Constitution dating from the Augusto Pinochet dictatorship. These continue as Chile struggles through the economic consequences of the COVID-19 epidemic. Bankers envisage an 8–14% GDP fall this year, the worst economic contraction in the country for 35 years.

'People thought that Chile was an upper income country, but we have a large population living in poverty,' says Patricio Navia, Professor of Liberal Studies at New York University and Professor of Political Science at Diego Portales University, Santiago, Chile. 'After COVID we do not have the resources to finance the energy transition, there are more urgent needs now.'

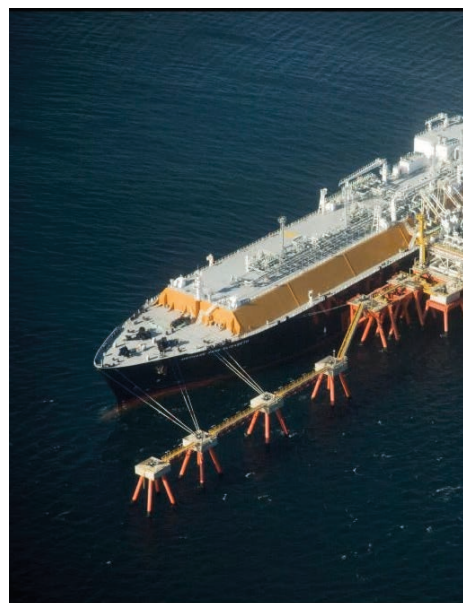
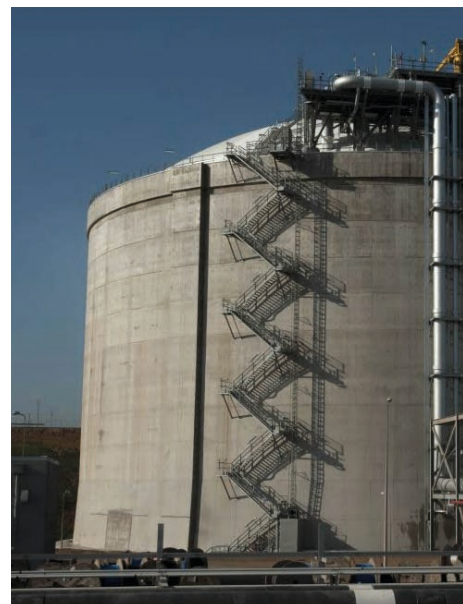
In response to the rioting, the government withdrew the metro fare and electricity rises and announced a \$5.5bn reactivation plan. This was followed in March 2020 by an \$11.75bn (4.7% GDP) stimulus package and in May by a \$23.93bn line of credit from the International Monetary Fund (IMF).

## Oil and gas problems

In July this year, state oil company ENAP shut in its 116,000 b/d Bio Bio refinery for two months' maintenance and laid off 14% of the workforce. The 94,000 b/d Aconcagua refinery meets 60% of national refined products demand, with the remainder coming from stocks and imports. In a July presentation to the senate, ENAP General Manager Andrés Roccatagliata announced that the company would cut capital investment by 40% this year (about \$400mn), halt all exploration drilling, renegotiate contract costs, eliminate all travel and external consultants, and seek to refinance

Prior to the pandemic, Chile's gas sector was expecting a growth year, with the Quintero (pictured) and Mejillones LNG import terminals constructed in the aftermath of the 2008 energy crisis operating at full capacity

Photos: GNL Quintero



\$620mn of debt. A future company restructuring, and possible privatisation, are rumoured.

Meanwhile, ENAP officials are facing a series of charges from local prosecutors about toxic emissions from its refineries and port facilities. In July, ENAP President Maria Loreto Silva, who was Minister of Public Works during the first Piñera administration (2010–2014), resigned because of alleged conflicts of interest in a land deal. She was replaced by Fernando Massú, already an ENAP Director and Chairman of the Santiago office of Brazilian finance company BTG Pactual.

Prior to the pandemic, the gas sector was expecting a growth year. The Mejillones and Quintero LNG import terminals – constructed in the aftermath of the 2008 energy crisis – were operating at full capacity. Gas accounts for 20% of Chile's power generation capacity. In 2018, Chile and Argentina signed a deal to revive mutual gas trade after a 10-year hiatus and to promote gas integration between the countries. But environmental protests have halted a number of local gas pipeline projects to power plants aimed at substituting coal-fired power. Low oil prices and COVID-19 caused operators of the Argentine Vaca Muerta shale play to cut operations and in May to suspend gas exports to Chile. Now there is substantial closed-in gas capacity in the power generation system.

#### Incentives

Enel Generation Chile, the local subsidiary of the Italian power utility, is committed to advancing renewable energy and plans to add 2 GW of renewable capacity to the system by 2022. Enel's 128 MW Bocamina coal-fired plant will be disconnected in December this year and the Bocamina 11 plant (350 MW) will shut down in May 2022.

At a June 2020 conference organised by the Santiago office of BTG Pactual, Enel Chile CEO Paolo Pallotti said that the evolution of natural gas prices over time will be crucial to renewables expansion, as will be the need for greater transmission grid flexibility. Gas industry grouping Asociación de Empresas de Gas Natural (AGN) issued a late June statement noting that incentives and 'adequate remuneration' for the utilities are key to ensuring the nation's decarbonisation plans.

An Enel Chile spokesman declined to comment on how the company expects the renewables projects will affect end-user tariffs

and how necessary improvements to the power transmission grid will be financed. However, in June the Energy Ministry announced plans for a 'fair and sustainable transition strategy' to address the socio-economic consequences of decarbonisation. At least 14,000 direct and indirect jobs in the coal-fired power sector will be lost as a result.

#### Public transport cross-subsidies

The 4% metro fare rise aimed to cover converting the system's power supply to 100% renewable energy, as well as subsidising fares on the city's expensive electric buses, newly purchased from China but without any bidding process that could have lowered their price. However, Santiago metro fares account for 15–20% of the net earnings of Chileans on the minimum wage and who make up a large proportion of its passengers.

Chile has no direct energy subsidies. The initial protests exploded into the largest such protests in Chile's history. Demonstrators were angered by the poor quality of public services, specifically energy and water utilities, and social inequality. The government acceded to demands for a plebiscite (direct vote of all members of the electorate) on reforming the constitution – scheduled for October this year – but which has left the entire political class entangled in a factional war. The outcome of this struggle may bring significant change to Chile's energy sector.

#### Constitutional questions

Chile's 1980 Constitution was designed to obstruct democracy. But since democracy was restored in 1990 there has been democratic consolidation, economic growth and poverty reduction. However, the core of the Constitution – namely individual property rights and the role of the state as a promoter of business and investment – remains the same.

Although Chile's scant oil and gas reserves remain the property of the state, electrical transmission and distribution services were handed over as a natural monopoly to private operators. Power generation functions as an open market. Electricity market privatisation in 1982 became a model for similar privatisation in Latin America and worldwide, notably Britain. But there have always been doubts how its minimal regulation could deal with the challenge of integrating renewable energies.

Countrywide lockdowns at the onset of the COVID-19 crisis left many consumers unable to pay their bills. In June, the Senate approved a controversial bill that forbids public utilities from cutting off access to basic services during the pandemic and created a constitutional hot potato. 'Companies purposely chose not to read meters in order to prevent the bill on non-payment going through,' observes Navia. President Piñera eventually vetoed the bill, but the veto was overturned by a congressional economic committee in mid-July.

#### Social versus business balance

The government views the senate's bill to prohibit the cutting off of basic services for non-payment as unconstitutional. According to Chilean lawyer Cristian Flores-Fernández, currently a researcher at the Humboldt University in Berlin, this unconstitutionality is based on the fact that it would affect the right to property, the principle of equality in relation to public burdens, and the right to develop economic activities by the utilities. The central axis of the constitutional discussion, Flores-Fernández says, will be a rebalance between social rights and social justice and existing property rights. The state has to protect access to basic services, he says.

The basic services issue coincides with discussions on a constitutional amendment to allow Chileans a one-off 10% withdrawal from their privately-managed Administradores de Fondos de Pensiones (AFP) pension funds. The government opposes this, although its governing Chile Vamos coalition is split on the issue. Economists claim that such a withdrawal would create an \$18bn fiscal hole in the budget, slump the capital markets and damage investor confidence – a crucial factor for the energy transition.

Navia believes that there could be a two-year process to write a new constitution that will put normal life, including the economy and investment, on hold and yield a document that is not substantially different from the present one. The political left wants to kill off the Pinochet legacy even though there is a need in Chile for a better balance between the state and the market. If the energy companies call for a tariff rise, the political left will call for their nationalisation, he says.

Changing Chile's energy mix while maintaining the same market dynamics will be a difficult, maybe impossible, task. ●

