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Will Chile's Power Sector Stymie Development?

Inter-American Dialogue's Latin American Energy Advisor

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Q and A: Will Chile's Power Sector Stymie Development?

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Chile was hit by three major blackouts from Sept. 24-26, halting operations at copper mines and darkening several parts of the country, including Santiago. The outages led to calls for the country to invest more in its power sector. Is Chile's power sector a weak link in the country's development? What needs to happen in the power sector in order to avoid future blackouts? Are problems in the country's electrical grid affecting its ability to attract businesses and investment?

A: Craig Kelly, vice president of The Cohen Group in Washington:

"Chile is blessed in many ways, with rich mining, forestry and agricultural resources. It is not, however, blessed with non-hydro conventional sources of power to fuel what has long been one of Latin America's most dynamic economies. Mining, in particular, demands high levels of power, a challenge underscored by recent blackouts. Chile has taken the right approach to its power challenges: diversification. The government and private sector continue to develop new projects in hydro, gas, coal, oil and non-hydro renewables. Even eventual small-scale nuclear power generation remains on the table. Diversification is essential because none is sufficient to provide even a majority of rising Chilean power demands, and each carries certain costs (expense, risk of drought, environmental concerns, uncertain regional politics, etc.) that must be balanced against the benefits. Chile has asserted leadership in the renewable energy sector, opening up a Santiago information center under the Energy and Climate Partnership of the Americas. At the same time, the International Energy Agency projects that by 2030, oil, gas and coal will continue to predominate in world energy consumption, and that each of these alone will account for a greater share than all renewable combined. Chile has no choice but to continue to develop conventional sources as well as hydro, and to balance benefits and costs in a diversified mix. Moreover, a February 2011 announcement by Chile, Colombia, Ecuador and Peru that the four countries would work to advance electricity interconnections was a sign that no country can afford to address power challenges in isolation."

A: Leni Berliner, chair of M3 Investment Group and president of Energy Farmsn International:

"Chile's energy regulatory system splits ownership of generation from transmission and distribution. As has occurred in other countries with this approach—originally adopted to encourage competition—this has resulted in under-investment in transmission and a complex

pricing and commercial environment for energy. Chile's four major grids are operated by private companies, which manage their purchase and sale of power in three markets: the regulated market (with prices charged smaller users set by the government every six months using generation and transmission cost data supplied by the operators); the unregulated market (larger users who can pay 'spot') and contract. The Chilean energy contract market is unusual in that supply contracts are not defined in terms of kilowatt hours delivered, but in financial terms. For these and other reasons, many large users have resorted to building their own generating capacity (and transmission lines under 100 kilometers in length). Add to this situation high growth rates in power consumption, estimated at 5 percent annually for the next decade or so and a policy of switching to 'alternative' fuels, especially wind and solar. The result is tremendous pressure to build new storage, transmission and distribution system. The country actually has reserve generating capacity; the problem is transmission. In theory, regulated prices now reflect the marginal cost of additional capacity increases, however to date Chile has not instituted a 'feed-in tariff' for new alternative, e.g. solar, producers. Such a tariff would be more effective at covering high capex and low opex installations, and would therefore attract more utility-scale solar developers to Chile. At present, solar power is being adopted in the north on a company- by-company basis, and this new capacity is not fed into the grid."

A: Rodrigo Fernández Hirsch, project manager at Energética in Santiago:

"These major blackouts hit Chile's principal electrical system, SIC, which supplies almost 80 percent of the country's demand. The three blackouts were caused by failures in important power substations of the trunk transmission system, and due to its operation and generation power dispatch, it was unable to withstand the failures. This situation exposes the fragility of the Chilean transmission systems that had been developed without proper planning. Actually, the transmission system planning is the responsibility of the authority who bids quadrennial studies for this purpose. These studies consider the demand growth and the generation availability, but the problem is that it considers only the minimum operation cost premise, so usually the system is underestimated. In Chile, transmission is a monopoly and a regulated activity. Transmission companies only make investments if the authority approves by decree the trunk system lines, otherwise they won't be remunerated. In this sense, the problem in the Chilean power sector is not a lack of investment, but rather bad policy planning of the authorities. Nowadays, important upgrades in the transmission system are being internationally bid, and it's expected that the new facilities will be ready by 2017. These issues shouldn't be considered as weak links in the country's development because we are working to solve them in a short period of time. However, regulatory changes might be needed to modify the way the electrical system's growth is being planned. Some could say that this situation affects Chile's ability to attract investment, but this is not that true because almost all the new business of international investors is on mining, in which projects take enough time to be carried out so that the system is in optimal conditions. Also, Chile is recognized as a secure country for investments, so some event with the electrical system won't change global perception of the country."

The Energy Advisor welcomes responses to this Q&A. Readers can write editor Gene Kuleta at gene.kuleta@thedialogue.org with comments.