

Introduction to the Issue on

How to Deal with the European Energy Crisis? Core Challenges for the EU

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Europe is in the grip of the most severe energy crisis in half a century. Triggered by Russia's invasion of Ukraine, it has laid bare how unprepared most countries were for such a shock, and how vulnerable their energy policies had made them over the years. While the shock may accelerate the transition to a more sustainable, secure, and resilient energy system, the severe impact on natural gas, coal, and electricity markets is driving energy prices to unprecedented levels. The high costs for energy make low-income households, SMEs and the industry in general face the coming winter with trepidation. The energy crisis will not be for a short term in Europe. If anything, the winter of 2023-24 is expected to be even tougher. Energy-intensive industries fear for its competitiveness in the world, households for the loss of prosperity. European governments are eagerly seeking ways to defuse the situation by implementing short-term measures to protect consumers and firms from the effects of the crisis (e.g., gas and electricity price brakes, VAT cuts on gas, households' energy subsidies, and many more). While national solutions may entail the risk of a subsidy race in Europe, some measures can also undermine climate protection goals. Many governments in the EU are now taking longer-term measures, aimed at increasing or diversifying energy supply, accelerating structural change and promoting renewable energies, or even by extending the use of nuclear energy. Finally, Europe will succeed only if they cooperate closely.

The articles in this issue of EconPol Forum examine the causes of the crisis, analyze its effects, critically assess the strategies already in place, and propose new short- to medium-term energy policy measures to better address the current crisis and strengthen the EU's systemic resilience to energy market volatility.

According to *Andreas Goldthau* and *Nick Sitter*, the EU's traditional strategy (based on the liberal market model) for ensuring energy security has been challenged not only by the Ukraine crisis, but also because current EU energy and clean transition policies have become highly interventionist. Taking into account the political and economic trade-offs of each model, the authors posit future energy priorities and strategies.

Reyer Gerlagh, *Matti Liski*, and *Iivo Vehviläinen* find that a coordinated introduction of energy demand reduction would go a long way towards stabilizing the EU electricity market. They propose lowering the price cap to €1,000/MWh across the EU, as this would

save consumers money, would not harm supply, and would significantly reduce the need for redistributive measures.

Daniel Gros points out that, given that the global supply of natural gas is fixed in the short term, Europe can only replace the lack of Russian gas if it offers more than what consumers elsewhere are willing to pay. For this reason, EU policy should focus on how to save gas, not on how to protect consumers from the current high prices.

The European electricity system is currently under pressure, as it depends on natural gas to balance the grid and to meet demand. *Mathias Mier* predicts that electricity prices will be six times higher than they would have been without the current natural gas crisis. Germany appears to be better diversified in this context, and price hikes are expected to be less severe.

Svetlana Ikonnikova and *Sofia Berdysheva* shed light on the problem of short-term energy security and affordability in Germany, which is urgently seeking substitutes for Russian energy. They also examine the importance of the energy transition on Germany's vulnerability to energy price shocks, and its failure to take security considerations into account in its trade arrangements.

Finally, *Alari Paulus* and *Karsten Staehr* explain the Baltic perspective on the energy crisis, in which higher energy prices have led to very high inflation and lower growth. Although many of the current challenges apply to practically every country in Europe, they are particularly serious in the Baltic states because of their energy-intensive economies, large dependence on energy imports, and limited grid interconnectivity. The authors believe that short-term measures must limit extreme energy prices, while monetary policy must avoid exacerbating the cost-of-living crisis. In the short- and medium-term, diversification of energy supplies is a must.

We hope you enjoy this Policy Debate of the Hour!