

Policy Brief

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ENSURING SOCIAL EQUITY IN VIET NAM'S POWER SECTOR REFORMS

Viet Nam has been implementing long-term reform of the power sector to improve economic efficiency and meet rapidly growing electricity demand. Viet Nam is also committed to achieving environmental sustainability and mitigate climate change, and these objectives must be aligned with efficiency improvements.

Key issues

One of Viet Nam's key socio-economic achievements since *Doi Moi* has been a very rapid expansion of the power grid, currently reaching about 98% of households. This, together with relatively fast economic growth¹, resulted in rapidly growing demand for electricity, which requires further increase of power production.

Viet Nam's long-term power sector reform must gradually shift it towards market-based pricing with a view to improve economic efficiency. Major milestones in the sector's reform were the approval of the Electricity Law in 2004, followed by a road map toward developing a competitive wholesale electricity market in 2006. The competitive generation market was basically established in July 2012, and according to a revised roadmap, a fully competitive retail market will be achieved by 2030.

Viet Nam also issued the Renewable Energy Development Strategy in 2015² and committed to reduction of greenhouse gas emissions under the Paris Agreement of the UN Framework Convention on Climate Change³. These policies align with its commitment to phase out fossil fuel subsidies in the national Green Growth Strategy⁴. Substantial reductions in electricity subsidies have been



observed for the period until 2014⁵ and this is expected to be maintained especially because the Government will not accept further rises in public sector debt. State-owned Enterprises also carry debt and Electricity Viet Nam (EVN) reported very substantial losses in the first half of 2016⁶. The last increase in power tariffs took place in May 2015 but as a result of these policies and developments taken together, an increase in power tariffs in 2017 and later seems inevitable.

Viet Nam's planned significant expansion of power generation capacity will mainly be generated by fossil fuels plus small increases in renewable energy, as expansion of (cheaper) hydro-electricity

¹ Viet Nam's economic growth rate averaged 6.4% per year in the 2000s

² Prime Minister Decision 2068/QĐ-TTg, 25 November 2015 on approval of the Viet Nam Renewable Energy Development Strategy up to 2030 with an outlook to 2050

³ Intended Nationally Determined Contribution of Viet Nam. Submitted to the UNFCCC in 2015. <http://www4.unfccc.int/ndcregistry/PublishedDocuments/Viet%20Nam%20First/VIETNAM'S%20INDC.pdf>

⁴ Prime Minister Decision 1393/QĐ-TTg National of 25 September 2012 on approval of the National Green Growth Strategy 2011-2020 with outlook to 2050

⁵ Subsidies declined from \$4.3 billion in 2012 to \$0.7 billion in 2014 (in 2013 dollars), which accounted for 0.35% of GDP in 2014 (IEA 2015 <http://www.worldenergyoutlook.org/weo2015/>)

⁶ <http://www.vir.com.vn/evn-reports-massive-loss-in-first-half-of-2016.html>



is not possible⁷. This, together with the possible phase-in of a carbon fee⁸ will exert further upward pressures on electricity prices.

Policy Implications

To ensure social equity, power sector reform has been complemented with various mitigation measures to protect low-income groups against rises in electricity prices.

To protect the poor and low income households against increasing electricity costs, various mitigation measures have been implemented in the past, including a lifeline tariff and a cash transfer scheme. Specifically, (i) beneficiaries in off-grid areas received an annual cash transfer for fuels as an alternative to electricity; (ii) poor and low-income groups in on-grid areas were charged at the lifeline tariff rate if they consumed less than a threshold of 50 kWh for three consecutive months and were registered. In addition, the poor also received a monthly cash transfer of 30,000 VND.

However, in mid-2014 two major changes were made: the Government (i) eliminated the lifeline tariff and initiated a subsidy for the poor

⁷ The Prime Minister Decision No. 428/QĐ-TTg of March 18, 2016 on approving adjustments to the national electricity plan in the 2011-2020 period and vision to 2030, according to which coal-fired power shares will increase from 29% currently to 49.3% in 2020 and 53.2% in 2030 while hydropower will decline from 40% currently to 25.2% by 2020 and 12.4% by 2030

⁸ A carbon fee was announced in the Viet Nam Renewable Energy Development Strategy

and special groups of beneficiaries⁹, which is a monthly cash transfer equivalent to the price of the first 30 kWh/month (with the condition that they consume less than 50 kWh/month); (ii) regulated a substantial rise in the first block tariff. The adjustment of the incremental block tariffs (IBTs) in Viet Nam has led to a reduction of cross-subsidies between different groups of residential customers. These changes impose more stringent requirements on precise identification of the poor, near-poor and social assistance beneficiaries in order to implement mitigation measures effectively as well as avoid burden on the government budget linked to leakages.

The current design and implementation of mitigation measures suffer from a number of serious shortcomings

- First, **there are numerous vulnerable people who are excluded if they are:** (i) not on the official poor list (e.g. migrants); (ii) the near-poor; (iii) social assistance beneficiaries who cannot prove that their usage is below 50 kWh per month; and (iv) unregistered users who are very poor in electricity consumption;
- Second, **the current benefit is too low**, particularly for those who have no access to electricity
- Third, **the cash transfer is costly to administer and imposes burdens on recipients.** High transaction costs relative to the level of benefit raise serious efficiency concerns.

⁹ Including non-poor social assistance beneficiaries who consume at most 50 kWh/month, social assistance beneficiaries and ethnic minority households living in off-grid areas

- Fourth, **the cash transfer cannot be delivered in a timely manner** to help people in hardship: even when the transfers are planned for the year, the budget is not transferred all at once, but quarterly; the officers must wait for the electricity bills or the accessibility of the households to the payment. These factors underpin the basic dysfunctionality of the current payment and reporting system.
- Fifth, **manual processing results in a great burden of reviewing work and high administrative costs, as well as potential mistakes.** For instance, in order to make the payments, the commune officer makes a list of the signatures of the beneficiaries and collects electricity bills as documentation for the payments. In the context of limited number of staff, which results in exclusion.
- Sixth, **dissemination of information to beneficiaries regarding the cash transfer policy has not been effective.** Many people in the countryside seem to not be fully aware of the objective of the support, which it is to protect them from electricity price increases. This undermines the objective of mitigation measures and winning wide public support for power sector reform.
- Finally, **there are no outcome indicators or performance indicators** for monitoring and evaluation, resulting in the absence of effective feedback and proper and timely adjustment of the mechanisms.

Possible ways forward

The mitigation measures in the current design and implementation cannot be justified on both efficiency and equity grounds¹⁰. To effectively and efficiently protect low income groups from expected further rises in electricity prices in the transition toward a full retail power market and low carbon economy, a new mechanism of mitigation measures with the following elements is suggested:

- For people who are connected to the power grid, the eligibility criterion for support (consumption of less than 50 kWh/month) is dropped, and the tariff structure would be made increasingly progressive:
 - the concessional first 30 kWh/month is retained, with two policy options:
 - set at a minimal price for all electricity users and the cash transfer is eliminated¹¹; or
 - the current tariff for the first block is frozen until 2020, and the current cash transfer is integrated into other

¹⁰ Six scenarios of IBTs proposed by EVN in September 2015 are to simplify the current tariff structure, keep the average retail price unchanged as well as to reduce cross-subsidy between customers, narrow the price gaps among blocks, and minimize changes in current IBTs. However, our analysis finds that neither the current 2015 IBT nor other scenarios of IBTs are pro-poor policies.

¹¹ Set very low - e.g. Egypt (1 US cents (=VND224)/kWh for the first 50 kWh/month); Pakistan (2 US cents/kWh for the first 50 kWh/month); and Sri Lanka (2 US cents/kWh for the first 30 kWh/month) (see https://en.wikipedia.org/wiki/Electricity_pricing#Price_comparison).

social assistance programs. This helps to ensure that all households can consume at least 30 kWh/month of electricity – the level commonly perceived as the energy poverty level.

- And the cost of this is covered through higher charges imposed on the other blocks:
 - the next 70 kWh/month is kept similar to the current IBT (i.e., VND 1,484 for the 31st to 50th kWh and VND 1,533 for the 51st to 100th kWh) in order to minimise the impact on the poor and the near-poor;
 - the final block (more than 100 kWh/month) will have a tariff of VND 2,748/kWh. This tariff would mean that EVN's revenue from the residential sector is unchanged, making this proposal financially feasible;
 - future increases will fall on the second and particularly the third block to meet three objectives: (i) efficiency; (ii) sustainability (financial and environmental); and (iii) equity.
- For people who are not connected to the power grid, energy subsidies should be set up at the level that enables the beneficiaries of social assistance to consume alternative

energies equivalent to 30 kWh/month electricity.

- Performance indicators should be established; monitoring and evaluation of policy should be conducted, and better coordination among partners in policy implementation is needed.
- Communication of policy changes should be considerably improved to win wide public support.
- The power sector should aggressively explore the possibility of scaling up the production of alternative forms of energy such as wind and solar power. This is developing rapidly thanks to technological breakthroughs leading to lower cost power plants and the possibility of "distributed" (local) power production through which consumers can reduce their electricity bills, equally local mini-grids can help remote communities and islands to improve access to energy¹².

¹² Cost of production of solar energy declined by 70% during the 2009-2016 period, and both wind power and solar Photovoltaics (PV) are expected to outperform coal and gas based power in a steadily increasing number of countries based purely on price. (REN21, 2016. Renewables 2016 Global Status Report. <http://www.ren21.net>)

*Fossil Fuel Fiscal Policies and Greenhouse Gas Emissions in Viet Nam – UNDP Research and Policy Dialogue Phase IV
"Short-term pain for long-term gain" – Assessing the effectiveness of the reformed Incremental Block Tariff and cash transfers*

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