



ENERGY COOPERATION BETWEEN ALBANIA AND SERBIA

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Background

The energy sector constitutes one of the most strategic sectors of the economy, which is part of the EU policy recently framed as Energy Union. The Western Balkan is considered an important area for the diversification of the energy production and transmission in Europe. This region increases the chances that the EU attains energy security. It has been a long term concern of the EU to reduce the energy dependency from external countries such as Russia. On the other hand, as in the case of most EU policies, the Energy Union and the relevant *acquis* on energy aim to initiate market reforms in the energy sector, to reduce

the monopoly position of firms and state subsidies, and enhance cooperation on energy trade and exchange between countries as well as aim towards a coal-free energy production in a sustainable environment mostly based on renewable energy. The alternative projects of reaching self-sustained energy production and diversity through investing in coal-based projects by refurbishing old technology plants and power grids as the Chinese investments in the Western Balkan region show, do not lead to long-term sustainable cooperation and could possibly jeopardize the structural reforms needed and the approximation of

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the EU acquis in the energy sector for the Western Balkan countries.

Prior to the Connectivity Agenda of the Berlin Process that has given priority to infrastructure and energy connectivity projects among Western Balkan countries, the general framework of inducing reforms in the energy sector has been the Energy Community Treaty which Albania and Serbia, as Western Balkan countries, are contracting partner signatories since 2005. According to the Energy Community Treaty, the Western Balkan countries, such as Albania and Serbia need to unbundle monopoly positions of state ownership in the energy sectors, create a market for energy trade and adopt the regulatory framework of the EU. Henceforth, the energy policy has received the attention and has been monitored by international organizations and EU institutions. To some extent, it can be argued that the energy sector has, in comparison with other sectors of the economy, a propensity towards yielding positive effects and sustainable results only through cooperation. At the same time, it is an economic sector of import for economic growth, and a precondition, due to energy security, of investments and competitiveness of the national and regional economic area. The EU enlargement strategy has foreseen the positive impact in trade,

employment and economic growth as a result of the interconnection of EU candidate countries energy networks in the EU energy network.¹

Nonetheless, the condition of the energy sector in the Western Balkan countries and more specifically in Albania and Serbia requires further improvements and reforms. Both countries need to diversify the energy production investing in energy security, on renewable energy and become integrated in the regional and European market. These processes go hand in hand with the necessary structural reforms of the economy in the energy sector mentioned above. The energy sector in Albania and Serbia has suffered from inefficiency, low capital investments, absence of self-sufficiency, more so in the case of Albania, and not being conducive to the protection of the environment as in Serbia.

This policy brief addresses the current situation in each of the countries with regard to the energy sector and specifically to its components, including electricity, natural gas, oil and renewable energy. Another part of the policy brief discusses the conditions of regional and European network cooperation in energy policy given the role of international organizations, existing energy international projects that have an impact on the two countries' 'energy package' as well as in the region. The policy brief discusses the recommendations regarding the cooperation on energy sector between Albania and Serbia.

¹ Popovici, Vlad: Energy Sector Progress and Setbacks for Balkan States Noted in the EC 2011-2012 Enlargement Strategy Package.

State of Play

Electricity

The electricity sector in both countries is characterized by potential improvements and existing problems. One aspect of the problems is related to the structure of this part of the sector. According to expert reports² the electrical power infrastructure, has gone through certain difficulties which have been fixed in the last years. Specifically these structural problems relate to limitations in transmission systems, insufficient metering and unpaid bills³ as well as depreciated infrastructure and old technology⁴. Another feature of the electricity energy in the Western Balkans has been the increase of the electricity consumption demand, primarily due to household consumption⁵. In the case of Serbia the consumption demand has been countered by the use of coal and lignite, which has led this country to

reach considerable levels of energy self-sufficiency, yet producing damage to the environment. In Albania, the hydropower energy⁶ is mostly used to produce energy compared to other sources.

Despite the fact that hydropower would be more preferable to coal for energy production, the main concern is the absence of energy security and self-sufficiency and the existing structure of the energy mix in Albania. "The hydropower output is highly dependent on the hydrology of a given year."⁷ Recently there has been an increased awareness of the need for reforms in the electricity generation and infrastructure in Albania. The government indicates that there has been under-investment, losses in the distributional network of electricity and low-payment.⁸ However, self-financing of the electricity part of the energy

² International Energy Agency, *Energy in the Western Balkans: The Path to Reform and Reconstruction*, 2008.

³ International Energy Agency, *Energy in the Western Balkans: The Path to Reform and Reconstruction*, 2008, p.124

⁴ *Ibid*, p.131

⁵ Residential demand accounts for 76% of total electricity consumption; industry accounts for 20% and other sectors 4%

⁶ Bechev, Dimitar: *The EU's Energy Union: An Opportunity for the Western Balkans*

⁷ Popovici, Vlad: *Energy Sector Progress and Setbacks for Balkan States Noted in the EC 2011-2012 Enlargement Strategy Package*. 2011, p.142

⁸ Rama, Edi. *Speech of the Prime Minister at Atlantic Council Summit on Energy and Economy*, retrieved at <http://www.kryeministria.al/en/newsroom/speeches/albania-as-important-link-in-the-european-energy-corridor1447950754>

sector is not the same as energy self-sufficiency. For almost more than a decade, Albania has entered the group of the Western Balkan countries that are importers of electricity. One reason for this condition is that the domestic gas and oil production has been restricted⁹ with no direct impact in the energy self-sufficiency and energy safety. On the other hand, the renewable energy despite the potential, such as wind, solar energy and bio-mass has not properly materialized. One possibility that can enhance energy self-sufficiency is the integration of the local electricity networks in the electricity networks of the region.

According to energy experts, Albania is facing complex structural problems¹⁰ and on the other hand there is no concrete effective substitutability of the energy sources given that the production and the consumption of natural gas and coal is low¹¹. Certain conditions limit the electricity sector in Albania. On the other hand, Albania as a net importer of electricity has been part of the electricity network that includes the neighboring countries of Greece, Montenegro and Kosovo¹². The renewable

energy due to the production of energy from hydropower constitutes one of the potentials of a sustainable development of energy supply and security in Albania. Nonetheless, overcoming the limitations and taking advantage of local potentialities could hardly be achieved without regional cooperation.

The electricity sector in Serbia has, according to the experts a potential to become a locus of energy transit and transmission¹³. As in the case of Albania and in other countries of the Western Balkan region, a diversification of energy sources and investments in this capital-intensive sector of the economy that could enhance the productivity of the supply and integration into the regional market are needed. As it was mentioned earlier, in terms of energy production, Serbia has relied on lignite which is considered to be costly and limited through time due to low productivity of the lignite reserves.

An advantage of the Republic of Serbia in the electricity sector, which is related to the country's position in the energy transit as a net exporter, is the fact that

⁹ International Energy Agency, *Energy in the Western Balkans: The Path to Reform and Reconstruction*, 2008, p. 124

¹⁰ Ibid, p.122

¹¹ Ibid, 124

¹² International Energy Agency, *Energy in the Western Balkans: The Path to Reform and Reconstruction*, 2008, p.140

¹³ Ibid, p. 304

Serbia is well connected to the UCTE transmission grids. In this respect, the energy infrastructure and the interconnectivity of the country to the broader regional and European energy network enhances the expansion of a market based framework and the inter-state, or regional cooperation.

On the other hand, there are still certain issues that need to be addressed. Serbia has low levels of exploitation of hydropower and bio mass energy production. Nonetheless there is the potential to substitute, at least partially, the use of lignite with renewable energy. In terms of the stakeholders involved in the energy policy, there is an existing experience that involves professional energy organizations and business organization in improving this policy, albeit not yet at the appropriate level.

Natural Gas

The natural gas component of the energy sector in Albania has experienced structural limitations that are related to de-industrialization process after 1990, limited exploitation of new natural gas resources and under-appreciated gas network

infrastructure within Albania. “Albpetrol sh.a” a state-owned enterprise indicates the issues that the natural gas sector is facing in Albania:

“The limited infrastructure of local gas is not operative in some parts and it requires large reconstructions and investments.¹⁴” At the same time, the interconnection of the local gas network in Albania with the international natural gas network has been absent¹⁵. The IAP and the TAP projects present a remarkable opportunity for the integration into the regional and international gas networks. Currently, the Albanian government has devised a strategy of the Gas Master Plan that considers the opportunities that arise for increasing regional and intra-state cooperation that would enhance the diversification of the energy production.

The profile of the natural gas production and consumption in Albania is characterized by low productivity and limited consumption only to refineries and oil fields.¹⁶ The integration into the regional IAP and the international TAP project presents according to the government’s strategy¹⁷ an opportunity to introduce in a larger scale the consumption of natural

¹⁴ <http://www.albpetrol.al/gazi-natyror/>

¹⁵ Ibid

¹⁶ Ymeri, Holta and Florian Xhafa., Third Actors in the Western Balkans and Energy Security, 2015, p. 20

¹⁷ <http://www.energija.gov.al/al/njoftime/lajme/masterplani-i-gazit-gjikhuri-piketate-zhvillimit-te-20-30-viteve-te-ardhshme>

gas for households by creating a gas market in Albania. On the other hand, Albania has considerable unexploited reserves of natural gas. The necessary unbundling of the monopoly position of “Albpetrol” in production and supply of natural gas has not become effective yet, albeit the commitment to do so as Contracting Parties of the Energy Community.

Contrary to Albania, the Republic of Serbia has a considerable energy mix. The market for the natural gas in Serbia is more extensive than in Albania. On the other hand, there is an increased consumption of gas by the households.¹⁸ The dominant firm in the gas market for transmission in Serbia is Srbijagas, which is dependent on the cooperation with Gazprom. According to experts’ reports, “Serbia covers more than 75 percent of its needs with Russian gas.”¹⁹ Serbia has an established natural gas national infrastructure and it produces natural gas partially on its own²⁰. The production of natural gas is administered by Petroleum Industry Serbia JSC (Naftna Industrija Srbije). The length of the transmission network

is currently at 2, 423 km according to the 2014 data.

Initially, with regard to international natural gas projects, Serbia supported the construction of the South-stream gas network in which the dominant stakeholder was the Russian Federation. For the time being, this project has not become effective and financial concerns have kept Serbia out of this project. On the other hand, Serbia has been successful in completing the required reforms in the natural gas market by adopting the Third Energy Package as a Contracting Partner of the Energy Community.²¹

Oil

It is estimated that Serbia’s oil and gas reserves amount to 14 million tons²². Oil reserves in Serbia are located mainly in the Vojvodina region and are owned exclusively by the company NIS Serbia, which on the other hand is owned by the Russian company “Gazprom”. Crude oil is mainly processed in refineries of Pančevo and Novi Sad. As per 2013, it was estimated that Serbia produced 16,840 of bbl/day,²³

¹⁸ Energy Community Secretariat, Annual Implementation Report 2015, p.181

¹⁹ CSS Analyses in Security Policy 2015, p.2

²⁰ Ymeri, Holta and Florian Xhafa., Third Actors in the Western Balkans and Energy Security, 2015 p, 13

²¹ Energy Community Secretariat, Annual Implementation Report 2015, p. 181

²² B92, All Serbian oil and gas reserves belong to Gazprom, Online: http://www.b92.net/eng/news/business.php?yyyy=2015&mm=01&dd=05&nav_id=92768

²³ CIA factbook, Online: <https://www.cia.gov/library/publications/the-world-factbook/geos/ri.html>

which made it the 75th oil producing country of the world. Currently the company NIS Serbia is expanding into the petroleum market of Bosnia and Herzegovina²⁴, a country with significant oil reserves.

Albania's oil reserves amount to 437.645.143 tons.²⁵ They are located mainly in the southwestern part of the country and the Patos-Marinza oil-field is considered to be the largest on-shore oil field in Europe. Albania's large oil resources started to be exploited during the late twenties of the last century. During the communist regime the oil industry of the country experienced a real boom by reaching the peak of 1,2 million tons of oil production per year²⁶. During the nineties, oil production, which was still at large under the control of the state owned company "Albpetrol", declined remarkably. However, during the last years Albania's oil industry has been experiencing a revival. For the time-being, oil production in Albania is in the hands of foreign companies such as: the Canadian "Bankers

Petroleum", "Stream Oil and Gas and Transoil Group", which have largely contributed to the recent growth of the Albanian oil production, reaching 1,368,000²⁷ tons as per 2014. Albanian oil is characterized as "heavy", which implies that it needs refining, in order to be considered fit for foreign markets. Albanian oil refineries, owned by the formerly state owned company of "ARMO", which underwent a contested privatization process, need to be modernized for being able to refine the domestic crude oil. This might be achieved either by alleviating "ARMO" from its financial issues, or by introducing new foreign investors interested in the Albanian oil refining industry. Experienced Serbian oil companies, such as "NIS Serbia", could play a role in this regard.

Renewable energy

Electricity produced from hydroelectric sources in Serbia, currently amounts to 26%²⁸ of the total production. The installed

²⁴ Oil&Gas Journal, "Exploration, production pace faster in Serbia, Bosnia and Herzegovina", Online: <http://www.ogj.com/articles/print/vol-110/issue-1a/exploration-development/exploration-production-p1.html>

²⁵ Albpetrol, "Rezervat Gjeologjike", Online: <http://www.albpetrol.al/rezervat-gjeol-ogjike/>

²⁶ Balkan Analysis, "Albania Oil Industry Enjoys Revival, but Investor-Government Relations Remain a Question", Online: <http://www.balkananalysis.com/albania/2012/02/05/albania-oil-industry-enjoys-revival-but-investor-government-relations-remain-a-question/>

²⁷ Albpetrol, "Prodhimi i Naftës", Online: <http://www.albpetrol.al/prodhimi-i-naftes/>

²⁸ The World Bank, "Electricity production from hydroelectric sources (% of total)", Online: <http://data.worldbank.org/indicator/EG.ELC.HYRO.ZS>

hydropower capacity is 2,835 MW²⁹, while hydropower generation is about 11,500 GWh. The largest part of Serbia's Hydro power potential, is concentrated at the rivers Danube, Drina, Velika Morava, Lim and Ibar. Other smaller rivers such as: Toplica, Crni Timok, Rasina, Studenica, Veliki Rzav, Mlava, Lepenac, provide for a minor part of the country's energy production. Hydropower in Serbia is generated mainly by its 16 hydro major power plants, which produce an average of 10.5 TWh/ per year³⁰. The largest hydro power plant in Serbia is the Iron Gate I (Derdap I), also one of the largest in Europe, producing 5,65 TWh/ per year.

It is estimated that only 0,2%³¹ of Serbia's electricity is produced by other renewable energy sources than hydro-electric power plants. As wind power is considered as a sector with huge potential for the future, Serbia's first wind-farm was inaugurated during 2015 in Kula

Vojvodina. The installed turbines have the potential to generate 3,3 MW³² of energy. Other ambitious projects such as the Belo Blato Wind-Farm³³ are set to become operational within the coming years. As in the case of wind energy, solar energy in Serbia is in its first steps. In 2014, solar energy produced in Serbia amounted to 5.232 mw/h. Serbia's biggest solar plant, with an output capacity of 2 MW³⁴, was built in Kladovo, during 2014. Serbia's biomass energy production is also experiencing positive developments. Currently six new biomass power plants with a potential of 6.32 megawatts³⁵, are being constructed in different parts of Serbia.

In Albania, electrical energy is produced exclusively by its Hydro-Electric power plants. As per 2014, the installed hydropower capacity amounted to 1,527 MW, while hydropower generation was at 4.01 TWh³⁶. Albania's hydro

²⁹ International Hydropower Association, Serbia, Online: <http://www.hydropower.org/country-profiles/western-balkans-serbia>

³⁰ Energy Sector Development Strategy of the Republic of Serbia for the period by 2025 with projections by 2030, Renewable energy Sources, Online: <http://www.mre.gov.rs/doc/efikasnost-izvori/23.06.02016%20ENERGY%20SECTOR%20DEVELOPMENT%20STRATEGY%20OF%20THE%20REPUBLIC%20OF%20SERBIA.pdf>. Pg. 15.

³¹ CIA Factbook, Serbia, Online: <https://www.cia.gov/library/publications/the-world-factbook/geos/ri.html>

³² Windpower Monthly, "Serbia installs first wind project", Online: <http://www.windpowermonthly.com/article/1372730/serbia-installs-first-wind-project>

³³ Windfair, Republic of Serbia - Green Star Alternative Energy to develop 20 MW wind power project, Online: <http://w3.windfair.net/wind-energy/news/5188-republic-of-serbia-green-star-alternative-energy-to-develop-20-mw-wind-power-project>

³⁴ Greentechlead, Serbia's largest solar plant opened in Kladovo, Online: <http://www.greentechlead.com/solar/serbias-largest-solar-plant-opened-kladovo-19455>

³⁵ Inserbia.info, Serbia to build six plants for biomass energy production, Online: <http://inserbia.info/today/2015/11/serbia-to-build-six-plants-for-biomass-energy-production/>

³⁶ International Hydropower Association, Albania, Online: <http://www.hydropower.org/country-profiles/albania>

reserves are mainly located at the rivers Drin, Mat, Devoll, Vjosa and Bistrica. It is estimated that Albania's hydropower potential is about 4,500 MW. The largest Hydro Power Plants are Koman HPP with installed capacity of 600 MW, Fierza HPP 500 MW and Vau i Dejës 250 MW, all of them located in the Drin River Cascade. Albania's largest HPP-s are mostly owned by the state, while small HPP-s are run by private companies. Meanwhile, an increasing number of foreign companies have been able to gain concession contracts for the construction of a series of HPP in Albania, such as: Ashta HPP, built by the Austrian consortium EVN&Verbund, with a total capacity of 50 MW and Devoll HPP with a total capacity of 280 MW, which is being built by the Norwegian company "Statkraft"³⁷. Albania's coastal lowlands, the hills in the Northern part of the country and the mountains in the South constitute perfect conditions for the construction of Wind Farms. So far, the first wind farm in the country will be established in the Kurbin area by a private company, which

is set to invest 54 million Euros in 12 wind turbines³⁸ that will have a total capacity of 36 MW. Although the Albanian government plans that by 2025, 4%³⁹ of the electric energy produced in the country, should derive from its wind farms, few investments have been made in this sector. As in the case of wind energy, solar energy in Albania has a lot of unexploited potential. Due to its Mediterranean weather, Albania enjoys long days of sunshine during its summer and spring seasons. However until now, solar energy has been harvested only by individual households, which use solar panels largely for domestic hot water needs. Projects, such as: The Country Program of Albania under the Global Solar Water Heating Market Transformation and Strengthening Initiative, supported by the Albanian government, GEF and UNDP, have made possible the installation of 75,000 m²⁴⁰ of solar thermal collector area into the facilities of different Albanian public institutions. The project aims to install 520,000 m² of collector area in different public schools and other social public institutions by 2020.

³⁷ Statkraft, Devoll Hydropower, Online: http://www.devollhydropower.al/new/?page_id=7358

³⁸ Invest in Albania, EUR 52 million project to establish the first wind park in Kurbin, Online: <http://invest-in-albania.org/eur-54-million-project-to-establish-the-first-wind-park-in-kurbin/>

³⁹ Albania energy Association, Albania Wind Energy, Online: <http://aea-al.org/albania-wind-energy/>

⁴⁰ UNDP Albania, The Country Program of Albania under the Global Solar Water Heating Market Transformation and Strengthening Initiative, Online: http://www.al.undp.org/content/albania/en/home/operations/projects/environment_and_energy/the-country-program-of-albania-under-the-global-solar-water-heat.html

Areas of Cooperation

Cooperation in the energy sector between the two countries has been largely focused on electricity. During 2014, the energy transmitted from Serbia to Albania amounted to 2,305 GWh⁴¹, while the energy transmitted from Albania was at 663 GWh. Cooperation in this area has been intense during the last two decades, but lack of infrastructural capacities for enabling large volumes of energy to be transmitted, has been an obstacle for the further enhancement of the energy links between the two countries. The establishment of a common regional energy market in the Western Balkans is to be considered as a possibility to enhance energy cooperation between both countries. Furthermore, as the Western Balkans is considered a region with a rich diversity of yet unexplored renewable energy sources, the EU might intervene through a series of investments to increase the share of renewable energy in the two countries, by lowering their dependence on imports from abroad. Another incentive to the strengthening of the renewable energy sector comes from EU member states that are compelled by their legislation⁴² to gradually increase the share of energy

produced by renewable sources, thus driving them to import this kind of energy from other countries, such as the Western Balkan countries. Italy planned to invest in Wind Farms in Albania exactly for this purpose.

The European Union strategy of an Energy Union that increases the long-term independence of the EU from external sources of energy has given priority to the establishment of a regional energy market, primarily on electricity, in the Western Balkan region. The reforms in the energy sector are aimed to include market reforms, cross-border balancing and what is known as spot market development that consist in creating a market for the buying and selling of electricity. All these measures are known as soft measures in the energy sector that would enhance in the future the integration and sustainability of the regional market into the EU market. Henceforth, the transformations are expected to take place at the national and regional level at the same time. In terms of the implementation of these reforms, Albania and Serbia have progressed at different paces. In terms of the regional capacity allocation, Albania has shown more progress by allocating cross-border

⁴¹ Energy Agency of the Republic of Serbia, 2014 Energy Agency Report, Pg.25.

⁴² Bankwatch Network, Western Balkans Electricity Plans: Where will that power go?, Online: <http://bankwatch.blogactiv.eu/2015/03/23/western-balkans-electricity-plans-where-will-all-that-power-go/>

capacity in the electricity sector with Montenegro, Greece and Macedonia. These steps have further developed after the Vienna Summit⁴³. In terms of the establishment of electricity energy market, Serbia has made more progress in removing legal and regulatory obstacles⁴⁴. However, the Energy Community reports indicate that both countries are far from the reaching the level of the cooperation between the neighboring countries and furthering the regional cooperation.

Another concrete mechanism that has evolved as part of the Energy Community with regard to the regional cooperation in the energy connectivity plans for the Western Balkans is the “Projects of Energy Community Interest” (PECI). The Vienna Summit of 2015, a sequel to the Berlin Process, has approved a number of projects that were proposed by WB6 members. These projects have been of national and regional nature. The energy sectors for which countries can apply include electricity generation, and infrastructure in gas, oil and electricity. Apparently, the dominant strategy of the members of WB6 including Albania and Serbia has been to promote through this mechanism, national projects. Even in the case of intra-regional cooperation in terms of electricity infrastructure, Albania has proposed

projects linking Albania with Macedonia, Kosovo and Italy. On the other hand, Serbia has focused on the thermal plants in the country and cooperating with Romania on the electricity infrastructure. Nonetheless, Albania and Serbia have initiated through the cooperation with Italy, the trilateral meetings that aim to improve regional cooperation between these countries also in the energy sector. Regarding the gas network and infrastructure the projects of 2013 approved at the Vienna Summit seem to follow different paths for Albania and for Serbia. The Republic of Serbia aims to interconnect with the Bulgarian Pipeline between Nis and Dimitrovgrad, as well as with Croatia. Albania, on the other hand is aiming for the construction of the TAP pipeline and the completion of IAP. The Paris Summit of 2016 has provided the possibility for a second round of PECI 2016 projects that involves the Western Balkan countries. Furthermore, the Paris Summit has given priority to the hydropower energy production in the region.⁴⁵ In this respect, apart from the energy exchange during peak season and due to Albania being a net importer of energy and Serbia a net exporter, the future focus on renewable hydropower energy could be a potential for cooperation between the two countries by reducing the dependency on coal.

⁴³ Towards a Regional Electricity Market from Vienna to Paris, Energy Community Secretariat 2016, p. 2

⁴⁴ Ibid, p.2

⁴⁵ Final Declaration by the Chair of the Paris Western Balkan Summit 2016 <https://wbc-rti.info/object/news/15157>

Policy Recommendations

- Both countries should work towards the achievement of energy diversity and move beyond national or local-based energy infrastructure projects as preconditions for sustainable cooperation
- Establishment of a regional energy market, along the energy stock exchange, which was already discussed in the Vienna summit by the EU officials and the relevant actors from the Western Balkans Region
- EU investments to the renewable energy infrastructure in Albania and Serbia and increased cooperation of both countries for joint projects in this area
- The establishment of a natural gas market in Albania after the inclusion in the TAP and IAP network could increase the interest of Serbian firms in investing in the distribution of gas networks in the household market
- Involvement of Serbian Oil companies in the Albanian Oil industry: Exploration of new reserves, exploitation and refining industry
- Increase of Albanian crude Oil exports towards Serbia
- An increasing role of Serbian companies in Albania's Hydropower sector, especially with regard to concession contracts for the construction of Hydro Power plants