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The EU ETS and large polluting industry

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Framework for the discussion

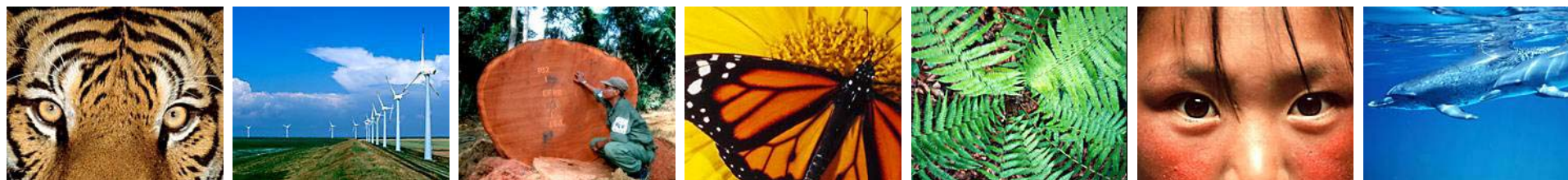
- Completion of the international agreement on climate change to stay below 2oC will **remove** competitive distortions associated with the EU ETS. So any discussion about support measures can only take place in the event of **an international agreement NOT being concluded**.
- EU ETS must have a transparent allocation system (full auctioning) so that it can transfer this design feature to all other ETS schemes to avoid competitive distortion.
- A carbon price signal can only be effective in a **transparent and competitive** market.





Problems with the current discussion

- Production costs do not cover the entire competitive position of an installation and company.
- There is a lack of integrity and trust in industry claims on competition.
- Any assessment must be based on **independently verified data** and account for historic investment trends, independently audited energy-efficiency reduction potential, accessibility to the market for competitors and possible financial support from auctioning revenue.
- **Free allocation is open to abuse**, costly and can subsidise the closure of European installations and investment in operations overseas.





The case for auctioning

Auctioning is “the simplest and generally considered to be the most economically efficient system... [auctioning] “eliminates windfall profits and put new entrants and higher than average growing economies on the same competitive footing as existing installations”. European Commission (SEC(2008)85-3)

Auctioning:

- Applies the ‘polluter pays principle’
- Ensures the full cost of carbon is factored into investment decisions;
- Avoids **windfall profits** to the most polluting sectors eg a report commissioned by WWF estimates that that windfall profits in Phase II (2008-2012) of the EU ETS for the power sector in Germany, UK, Poland, Spain and Italy alone may accumulate up to **71 billion Euros**;
- Provides carbon finance for investment in climate protection and wealth generation;
- Rewards the most efficient low carbon production.





Benchmarking does not work

- A Carbon Trust study concluded that with free permits “an incentive remains for these sectors (cement and steel) to reduce domestic production, sell the allowances and import substitutes or carbon-intensive intermediate products”.
Source: The Carbon Trust (2008).
- Impossible to set EU wide benchmarks for installations eg aviation ETS example as well as current N₂O case where the best available technology removes N₂O but the standard sets the benchmark to give permits to 2 plants.
- Data is commercially sensitive and open to gaming.





The case for cement starting with 100% auctioning from 2013





Criteria for assessment

- The criteria outlined below must be applied to all sectors to allow for a true discussion about alleged competitiveness impacts.

1. Trade intensity

2. Market structure/concentration

3. Installation level investment





European Commission overview

- “Due to the need of significant capital requirements, energy intensive industries tend to operate in fairly concentrated markets. Some of these industries have a significant track record of collusion and infringements of the competition rules. If companies prove to be able to increase prices by collusion, they can not be expected to have great difficulties in increasing prices to a similar extent when facing increased cost of emissions”. (European Commission 2008).





1a. Trade intensity

- Cement is cheap to produce. Main cost comes from the transportation of cement in bulk.
- Cement is largely produced for domestic consumption.
- Overcapacity in cement production facilitates export.

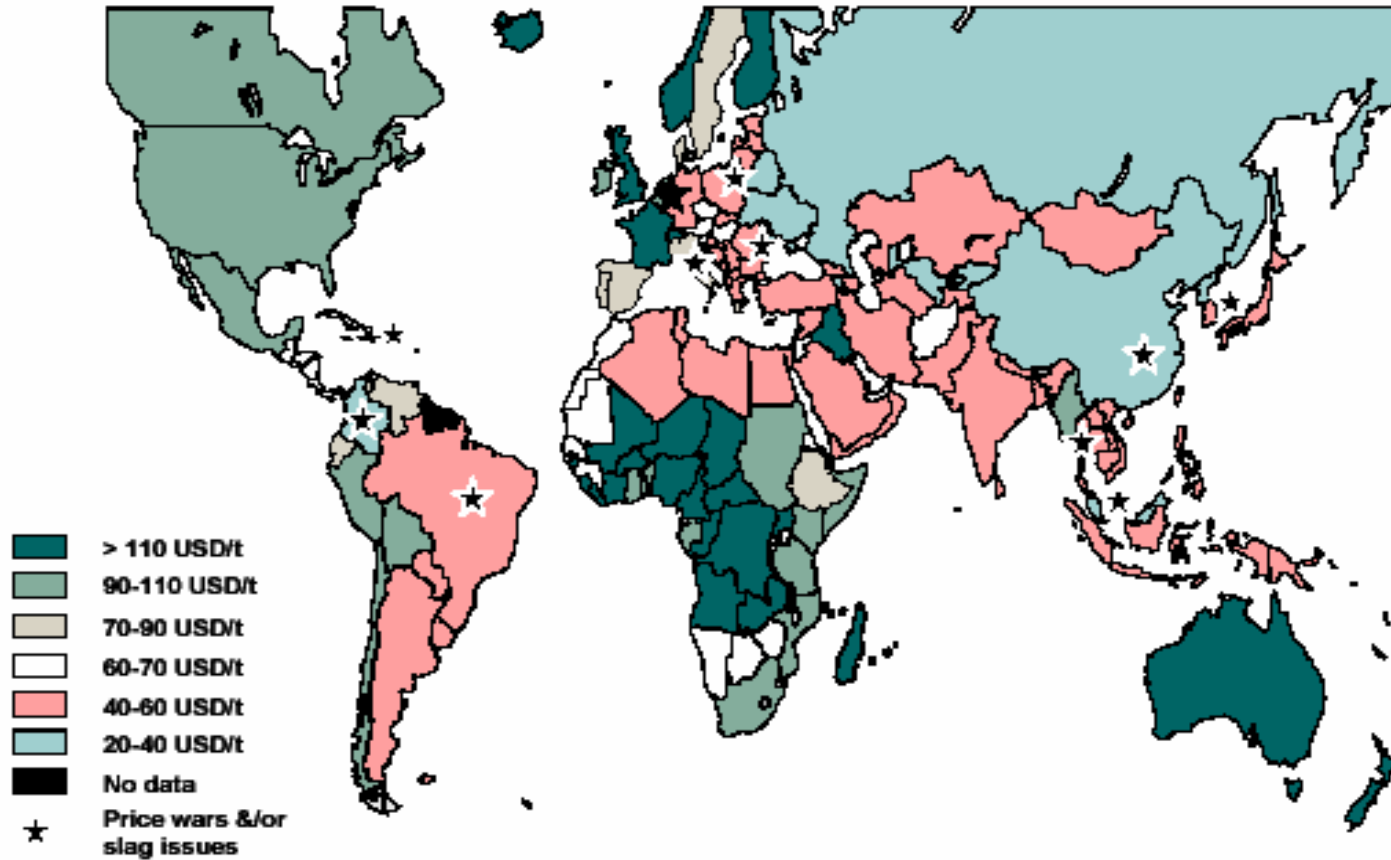
Key facts:

1. Only 8% of cement consumed in the EU comes from non-EU countries.
2. Current demand for cement imports comes from Italy and Spain. Local cement companies reduced production capacity which has led to increased demand for imports.
3. Egypt has a 11 USD per tonne of cement export tariff on to ensure that it is used in their countries.
4. The United States is the largest market for Chinese cement. Other customers include the Taiwan, Hong Kong, the Philippines, South Korea, Brunei, Malaysia, Vietnam, Singapore, and Macao. (WBCSD. 2002)





1b. Trade intensity (Major difference in global prices)



Source: Exane BNP Paribas estimates





2a. Market structure

- Cement - “market concentration in the cement industry is rather high and **prone to collusion** and formation of **cartels**”...“the cement sector is unlikely to be **significantly exposed to international competition** due to high transportation costs”. (European Commission 2008).





2b. Market structure

- Anti-trust and corruption cases:
 - (1994) **European Commission** fines cement cartels **13.5m Euro** and concludes “Anti-competitive practices and agreements constitute economic infringements designed to maximise the profits of the participating undertakings. The harmful effects for the markets and for consumers are particularly serious in the cement sector, since they are passed on to the construction and housing sector and to the real-estate market in general”. (European Commission)
 - (2002) **German government** smashed a major cartel in the cement sector with fines of **660m Euro**. (Guardian. 2002).
 - (1999) **Commission fined** 8 European steel companies (Corus, Mannesmann, Vallourec and Dalmine) were fined **99m Euros** for rigging stainless steel tubes market. (BBC. December 1999).
- Market control: ArcelorMittal reduced production to stabilise European steel prices in June 2007. This shows that the company sets the price, not a liquid market. (Steel Strip. June 2007).





3. Installation level investment: Arcelor steel plant in Liege, Belgium, 2003-2008

- Guy Dollé (CEO in 2003) announced that 6 smelters to be run down to closure. Investment focus on producing flat carbon products near coasts to maximise profits from exports to Asia.
- This decision was based on the conclusions of an in-depth study which took account of market shifts in prices and volumes, cost increases, the amount of investment required and environmental issues with the plant.
- 2007 ArcelorMittal decides to reopen the plant because of the high price of steel.
- Key points:
 - (i) The company made a business decision not to invest in the installation.
 - (ii) Current problem down to lack of investment from the company.
 - (iii) No impact on the overall profitability of ArcelorMittal.





Criteria for assessing competitive concerns if there is no international agreement

- An installation must present its case to an independent institution/ agency/process.
- Historic investment trends in an installation against historic investment trends across the company.
- Energy efficiency potential in an installation. This survey must be performed by a professional energy engineer.
- Demand for the installation's product in the region, country and internationally.
- Regional trade barriers – transportation costs, access to ports, output specifications,
- Low carbon production technologies and techniques
- Qualifications/skills and business achievements of the leader(s) of the installation (director, manager, foreman, employees, etc)





Conclusions

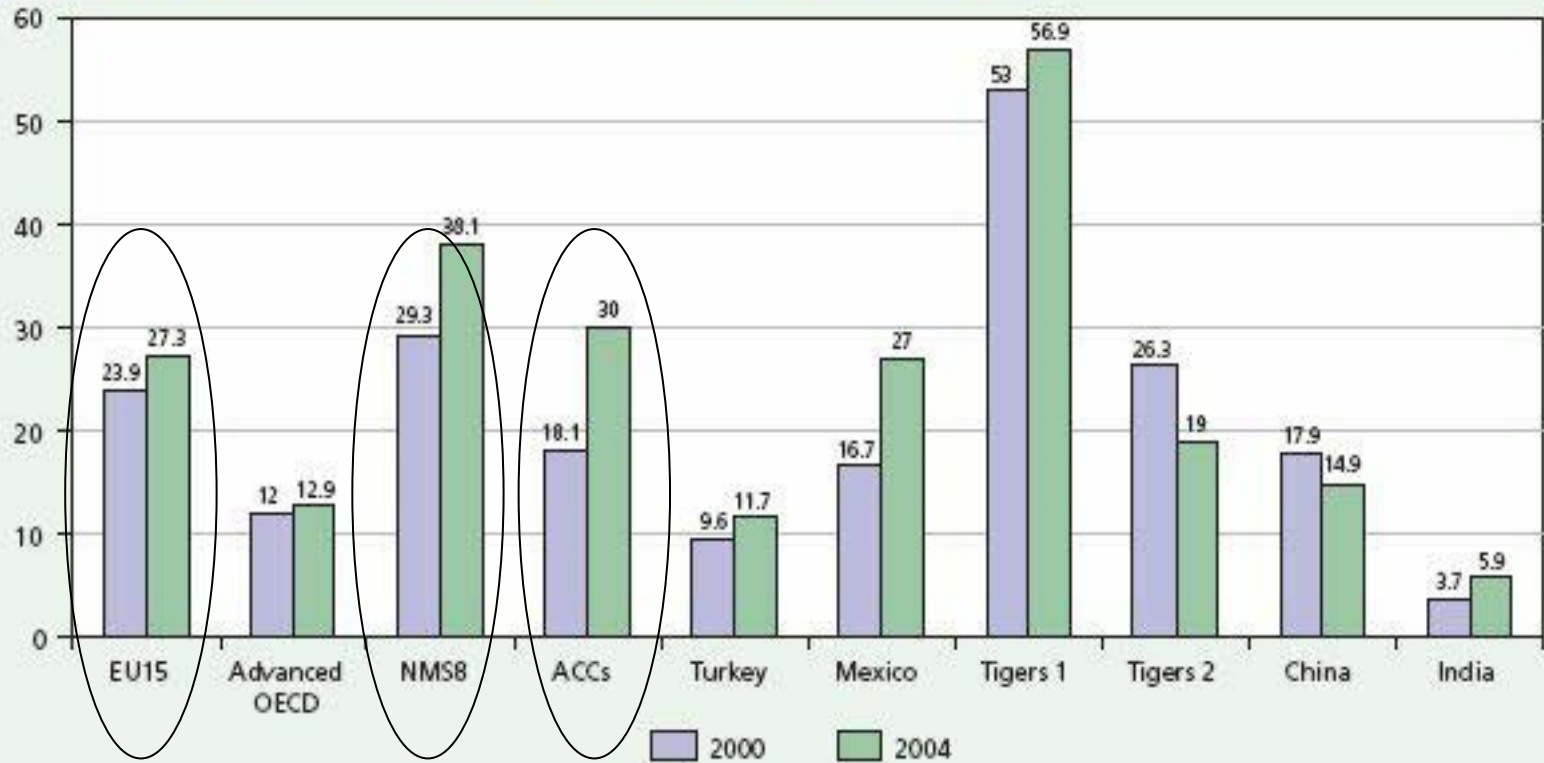
- Competitiveness concerns can only be considered **if there is NO international agreement.**
- If there is no international agreement on climate change then **an independent agency/institution/process should be set up to assess claims from an installation.**
- Large polluting sectors should be liberalised to ensure liquid markets, efficient production and consumer confidence.





Health of the European economy

Figure 1: The stock of foreign direct investment (FDI) in % of GDP, 2000 and 2004





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It's time to fight!!!!**



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