european aluminium association

6 November 2013

Q&A ON THE CUMULATIVE COST ASSESSMENT OF THE IMPACT OF EU LEGISLATION ON THE ALUMINIUM INDUSTRY

1. What is the background of the Fitness Check and CEPS cumulative cost assessment?

As defined in the European Commission's Communication on the mid-term revision of its Industrial policy (Oct. 2012), a sectorial fitness check assesses the impact that the overall policy and regulatory framework has on the competitiveness of a sector. The objective is to identify excessive administrative burdens, examine regulatory overlaps, gaps, and inconsistencies, and assess the cumulative costs impact of EU legislation over the past ten years (2002-2012). The findings review the existing legislation governing the sector and provide a basis for implementing future enabling policies. The aluminium, steel, and petroleum refining sectors have been identified as priority sectors for this new exercise.

The European Commission subsequently asked the research institute Centre for European Policy Studies (CEPS) to assess the cumulative cost impact borne by the industry and attributable to EU policies in the following areas: energy, climate change, environment, competition, trade, and products policies. The work started in May 2013 and the final report was published in early November 2013.

2. Why a "cumulative costs assessment" for the aluminium sector?

When the European Commission published its mid-term revision of EU industrial policy, **it acknowledged that the aluminium sector is "critical for the EU's industrial value chain** and urgently requires new investment to be made in the face of strong international competition."

This is because Europe's production capacity today is on a sharp decline despite an increase in demand both at global and European level. Demand for aluminium products is driven by the specific properties of the material and the delivery of forward-looking and sustainable solutions for a resource-efficient and low-carbon society. Between 2008 and 2012, Europe's primary production capacity of aluminium was reduced by more than a third

as a result of plant closures and curtailments. This has resulted in imports making up more than 50% of all aluminium used in the EU.

By closing down primary production, Europe loses more than economic activity and jobs. It makes **Europe dependent on imports** of a material that is strategic in many sectors such as, amongst others, aerospace, green transportation, renewable energies, efficient buildings, lighter & safe packaging, and high voltage network interconnection.

It also **increases working capital costs to manage supplies for the downstream/transformation industry** and isolates it from innovation clusters. Last but not least, this does not bring any environmental gain at the global level, as imported aluminium has on average a **higher CO_2 footprint**.

The semi-fabricators ability to **innovate is also deteriorating**. The needs for proximity, fast delivery, and the known quality of products are necessities for creating new products. Therefore, the European Commission decided that there is an urgent need to better understand the **cumulative impact of EU legislation** on the aluminium industry and to assess how the EU should better support this important sector against global competition.

3. How has the cumulative cost assessment been executed?

The cumulative costs assessment was made with surveys of industrial sites to ascertain data and impacts across the entire value chain. 46 plants - representing the main segments of the aluminium production process and supply chain - were surveyed in Europe (11 primary aluminium smelters, 20 secondary aluminium producers, and 15 downstream players). Both administrative, compliance, and direct costs were assessed, and regulatory costs were compared to production costs price-cost margin, EBITDA, price-raw material margin, and market price.

CEPS has worked for several months to complete this study which was finalised in November 2013.

The results clearly demonstrate that the aluminium industry is indeed negatively impacted by some EU policies and its global competitiveness has decreased when fully exposed to the costs arising from EU rules. Based on these findings, the European Commission will evaluate which measures should be taken to reverse the decline of the industry's competitiveness.

4. What are the key conclusions of the CEPS study?

This is the first time that a study demonstrates the cost of compliance with EU rules. Results show that these costs are very high for the aluminium sector and significantly impact its competitiveness. As other regions in the world do not face the same costs, and as sale prices are fixed globally on the London Metals Exchange (LME), the challenge is to maintain the industry within Europe.

In short, the study found that:

- Aluminium is globally priced on the London Metal Exchange and cannot pass on costs unilaterally imposed by EU rules. Plants that have to purchase their electricity on the market and are **fully exposed to the costs arising from EU climate and energy policies face an overall cost attributable to EU legislation of up to €228 per tonne of aluminium, i.e. 11% of total production costs** including raw materials (close to 20% excl. raw materials);

- EU plants that are still shielded from EU rules due to pre-existing long term electricity contracts face EU regulatory costs of 27 €/tonne;

- For most exposed smelters, the majority in the EU, the regulatory costs incurred by EU producers originate from the passing-through of energy costs and surcharges to support renewable and related grid costs (49%), Emissions Trading Scheme (ETS) indirect costs embedded in electricity bills (42%), and environmental costs (9%).

- The cumulative cost of EU rules and regulations ranged from 23% of profits in 2006 (the most profitable year) to 242% in 2011, when margins were lower because of the crisis;

- Regulatory costs amount to more than a third of the competitiveness gap with the lowest cost producers in the Middle East, which are among the biggest exporters to the EU;

- The impact for the downstream sector is more limited in absolute terms, but when compared to profit margins it is still significant. This has been particularly evident during the crisis, as margins have been lower. Secondary producers (remelters and refiners) – which in most cases are SMEs – are faced with ETS indirect costs are as high as €2.44 per tonne, and environmental legislation costs of up to €6.06 per tonne. These values are €7.09 and €3.06 per tonne for semi-fabricators (rollers and extruders respectively).

5. What are the next steps?

Over the past ten years, the European aluminium industry has continuously stressed the unintended consequences of certain EU policies and regulations. Our call to assess thoroughly the impacts of policies and to adjust regulatory instruments were often understated and ignored. For the first time, these implications are assessed and ascertained with actual data from plant surveys. The cumulative impact of EU climate and energy policies on our industry is significant and now also undisputable as it is backed up by facts.

Nevertheless, the de-industrialisation of entire European regions can be stopped. Pragmatic and rapid answers can be implemented to reinforce our industry's competitiveness, while at

the same time achieving energy efficiency and climate change objectives. There is firstly a need for political will and a clear direction. EAA will present to the European Commission a shared agenda for action, with a concrete set of measures to create an environment which would make investing in Europe a more attractive and viable option for the aluminium industry.

This issue needs to be high on the agenda of the EU Summit in February 2014 that will focus on the European industry's competitiveness and energy prices. High-level political commitments and a clear direction are expected from Heads of State and government.

Although the situation is concerning and urgent, we believe that it is neither too late nor impossible to secure growth and jobs in a way that contributes to the EU's climate and sustainability goals. The aluminium industry is ready and willing to be a part of the solution to reach those goals.

6. What concrete policy changes are needed?

Policy changes must be embedded in a clear and long term horizon which is an essential condition for long term investments. EAA is proposing to EU policy-makers a set of concrete policy measures to revive this strategic industry for Europe.
EAA calls for concrete policy measures to:

- Ensure competitive energy prices through sound industrial, climate and energy policies
- Secure availability of scrap, further unlock the recycling potential and foster Europe's circular economy
- Maintain the EU industrial value chain, promote innovation and boost demand for resource efficient solutions

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About the European Aluminium Association:
The European Aluminium Association, founded in 1981, represents the whole value chain of the aluminium industry in Europe, from alumina and primary production to semi-finished, end-use products and recycling. The European aluminium industry directly employs about 255,000 people and yields an annual turnover of 39.7 billion €. *For information, please visit www.alueurope.eu*

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