

EUROPEAN ECONOMIC COMMUNITY

Commission

ADDRESS BY MR. ROBERT MARJOLIN

VICE-PRESIDENT

OF THE COMMISSION

OF THE EUROPEAN ECONOMIC COMMUNITY

to the Institute for the Economics of
Energy at the University of Cologne

14 June 1962

X/5090/62-E

X

THE IMPORTANCE TO EUROPEAN ENERGY POLICY
OF THE GERMAN INQUIRY INTO ENERGY

Ladies and Gentlemen,

It is indeed an honour to be taking part in this twelfth meeting of the Institute for the Economics of Energy in Cologne University. My thanks are due in particular to the organizers for having invited me, and I am glad that their invitation reached at a time when the Commission was preparing to submit proposals concerning the lines to be followed in the Community's policy on energy. This provides an opportunity for me to put before an audience of specialists the Commission's ideas on the long-term solution of energy problems.

o

o

o

Before embarking on a discussion of these problems, I should like to compare the conclusions which emerge from the inquiry into their German aspect with those we ourselves have reached for the EEC as a whole.

The Economic Research Institutes participating in the German inquiry have produced a very full and instructive report, on which I warmly congratulate the authors. I am sure that a study of this nature will be very useful to the authorities of the Federal Republic when they have to decide on the elements of an energy policy appropriate to conditions in this country. For us in the Community, it sheds light

on a number of special facets of the energy market in Western Germany which might have escaped our attention in our more general approach to the problem.

On the whole, despite some differences of method, the conclusions reached by this inquiry are much the same as our own.

To begin with, as far as the growth of requirements is concerned, the inquiry estimates a 50% rise in the total consumption of primary energy by 1975, which corresponds roughly with the estimated increase for Germany in the studies made by the Commission.

The same applies for the way in which these needs will be met. It would be unreasonable in any case to suppose that coal output will exceed the current figure; in fact, it will probably drop below that level. So there will have to be more imports, particularly of petroleum, until nuclear energy can play an important role, and this can hardly be expected before 1970 or 1975.

Coal has a number of outlets that will remain: the iron and steel industry (for coke) and the thermal power stations at the pit heads. In the case of Germany this means about 85 million tons, or two thirds of today's output. Other outlets are more uncertain and will depend on the competitive conditions in which domestic or imported energy products will be available. Price will therefore be of decisive importance.

- 3 -

The inquiry for the Federal Republic concluded that mining costs in the coalfields were almost certain to go up. According to the report, a great deal can still be done to rationalize coal mining, particularly by further concentrating production in the most profitable workings, but this will hardly offset the increased costs that are likely to occur.

Coal experts in France, Belgium and the Netherlands have come to the same conclusion. Nevertheless, I would stress that the German coalfields have an advantage over those elsewhere in the Community, where conditions make it difficult to obtain equally high yields. In the common market, German coalfields should benefit from this situation.

More important is the price relation between domestic energy and imported forms of energy - American coal or fuel oil.

It seems difficult to question the stability of American coal prices, at least in the long term - that is, if we ignore the ups and downs in freight rates.

For petroleum products the question is more controversial and the opinions expressed have often been divergent.

The experts who conducted the inquiry feel no doubts on this point, and affirm that in future fuel oil should still further improve its ability to compete with coal.

I would like to give you more details on this point.

Although we must not underestimate the importance of the fields recently discovered in North Africa or the considerable reserves still available in the western hemisphere, the Community's principal source of supply will remain the Middle East, because of both the richness of its reserves and the low extraction costs obtaining there.

A conservative estimate puts the proven reserves of the Middle East at 26,000 million tons, which is two thirds of total world reserves and represents a hundred years of production at the current rate. Probable reserves are certainly much higher, and we may take it that the total reserves of the region in 1975 will be enough to supply Europe with oil for another fifty years even allowing for its increased rate of consumption and the additional outlets which may have been developed in the Far East or the western hemisphere. Reserves, then, seem to be more than adequate, and there is no room for fear on this score.

The price factor is more problematic. The actual prices of petroleum intended for Europe are significantly lower than the posted prices. It is quite normal for the producing companies to grant independent operators reductions of 15 to 20%. Sales by integrated companies to their subsidiaries are generally made at prices that do not differ so much from official prices, but on the markets of consumer countries these subsidiaries cannot charge more than the independents. Some people invoke these facts to stress the precariousness of the current price level and the risk of prices going up in the future.

Two comments can be made here. The first is that at this price level total demand is satisfied and that the oil companies can cover all their expenses while ensuring that their exploration and investment programmes are carried through. The second relates to the royalties that these companies have to pay to the governments in producing countries under existing agreements. In the Middle East, these royalties come to about five dollars per ton on an average posted price of 12.5 dollars. The governments of the oil-producing countries have always been opposed to reductions in the posted prices, which for them would mean losing revenue. There is a risk - and we cannot ignore it - that these governments may bring political pressure to bear so as to obtain a bigger share in the yield from the exploitation of their subsoil. This revenue, incidentally, is continually on the increase because of the rapid rise in production; between 1949 and 1960 it rose from 136 million dollars to 1355 million dollars in the four main producing countries in the Middle East.

If we leave this risk (which is really more political than economic) out of account, it seems that we can reasonably reckon with a supply of petroleum and therefore of fuel oil - the price of which depends directly on that of crude oil - on terms similar to those prevailing at present.

Another affirmation that has often been made is that the increasing use of imported fuel might endanger the security of supplies and that the maintenance of coal production at something like the current level would consequently be fully justified.

Now this conclusion is far from obvious. The problem of security will arise in any case, since the size of the foreseeable shortage is not such as will allow a variation of a few millions or even a few tons of

millions of tons of coal output to exert any significant influence on the degree of security. So this is rather a problem of petroleum policy, to which I shall return later. For the moment, suffice it to say that security has already been considerably strengthened by the discovery of new fields throughout the world and by the existence of excess capacity both in production and in transport. In a crisis, support could also be found in the form of imported coal. Lastly, the discoveries of natural gas in Europe and the Sahara, as well as the contribution of nuclear energy, will improve long-term security.

To buttress the security of supplies, it would be as well to diversify sources and to accept some increase in the price of imported fuels, both to finance adequate stocks and to enable sources to be tapped that might not always be the most economic but would help to spread and reduce political risks. Special precautions should also be taken in this context about imports from the Eastern bloc, should this volume ever be such as to put the Community countries in a dangerous position of dependence.

o

o

o

This is a brief summary of the facts. The analysis made by the Economic Research Institutes accords exactly - as I have already said - with our conclusions.

However, there are vast differences between the energy policies pursued by the various Member States. Although the situations in Germany, Belgium and France may be rather similar, because in those countries

- 7 -

considerable protection is given to coal, conditions are quite different in the Netherlands, where the coal industry is much less important, and even more so in Italy, which has always been dependent on imports.

It is quite normal that at an early stage each Member State should cling to its own methods in coping with the difficulties of the energy market, but we must hope that the desire to attain the common objectives laid down in the Treaty of Rome will mean that certain domestic difficulties are overcome and that, as a result, a common energy policy is adopted.

Our role, as the executive organ of the EEC, is to work for an energy policy that all Member States will recognize as the most favourable for the Community in the long run. In doing this, we must bear it constantly in mind that the proposals we make do not concern an isolated sector of the economy but are part of economic policy as a whole and may come to have a decisive effect upon that policy.

The EEC Commission has had long deliberations on this question and has come to the conclusion that the only really defensible policy is to ensure a cheap supply of energy and that this can be combined with ensuring conditions of adequate security.

Up to the present Europe has been an area in which fuel was expensive. The cost of producing coal is almost three times as high as in the United States; but the most significant factor is that Europe has only a small volume of natural gas at her disposal, while in the United States this accounts for more than one third of consumption and is industry's cheapest form of energy. Price differences are not so big for the private consumer, because fuel prices include a wide margin for

transport costs, but in the case of the supply of primary energy to power stations prices some years ago were almost twice as high in Europe as in the United States. This seems to reflect quite accurately the usual terms offered to industry at that time.

Prices have since come down, thanks mainly to the growing use of petroleum products, but quota restrictions, customs duties and taxes on consumption have until now prevented consumers from reaping the full benefit of these price cuts.

In the severe competition that will soon bring the European economy face to face with the other great industrial regions of the world, a reduction in the price of energy would be of great assistance to our industries. It has often been said that the share of energy in the price of industrial products is too small - 3 or 4% - to constitute a real advantage in competition, but in reality we should consider not only the energy consumed directly by each establishment (as in this calculation) but also the amount of energy which has gone into the production of the basic materials or semi-finished products included in the manufacturing process. This gives us decidedly higher percentages: more than 25% for iron and steel, 20% for non-ferrous metals, 10 to 15% for chemicals; in a processing industry like engineering, a figure of 8% can still be obtained.

Another element to be taken into consideration is that, for the industries which are heavy consumers of energy, the price of fuel is an important factor in the choice of a site. There are certainly other factors that may influence this choice - availability of labour, the level

of wages, the proximity of markets, etc. - but they are not always decisive, so that a significant difference in fuel prices may in many cases be the decisive factor.

If a given Community country should withhold the advantages of a cheaper fuel from its own industries, it would then risk forcing some of them to set up elsewhere, where the terms offered would be better.

Similarly, the maintenance of fuel prices at an artificially high level would mean that the Community's outlying regions would not receive the benefit of cheaper fuel from abroad and this would hamper the rational distribution of investments.

Apart from the aims of low cost and security, we must not lose sight of other questions, particularly of the social problems, which are of such importance in the case of coal mining. But I must recall that it will not be possible to find a satisfactory long-term solution to any social problem if basic economic rules are constantly flouted.

On 20 February 1962 the European Parliament adopted a resolution which had been proposed by its Energy Committee, of which the Chairman is Professor Burgbacher, to whom incidentally I would like to express my appreciation of his exceptional ability and authority in this field and also of the untiring effort with which he has expounded the cause of a common energy policy in the Community. The resolution of the European Parliament has expressed the principles of a common energy policy in the clearest of terms, and I cannot do better than to repeat them here:

- cheap supplies
- assured supplies,
- any change-over should be gradual,

- 10 -

- long-term stability of supplies,
- free choice for the consumer,
- unity of the common market.

What we now need is to build upon those principles an energy policy that will embody them in the best possible combination when it is applied in the various Member States.

o

o

o

As you know, the EEC Commission is directly responsible for petroleum, natural gas and electricity, while the High Authority of ECSC bears the responsibility for coal and the Euratom Commission for nuclear energy.

Before outlining how a common petroleum policy can be envisaged, I will give you a brief indication - and a pure personal one, since the matter comes under ECSC - of the lines along which a solution to the coal problem could be sought. Given the need for a cheap supply of energy, is the Community to maintain - for some time at least - its coal output at a higher level than would be permitted by the free play of competition without taxes, duties or quota restrictions ?

For several reasons I am tempted to say "yes". The first is that the future trend of the price of imported fuel is not known with enough certainty. Even if we can legitimately hope that imported fuel prices will remain at about their present level, the fact remains that under the pressure of external events those prices tend to rise and we might one day regret having abandoned productive capacity which,

though not competitive under present conditions, might eventually become competitive again as a result of a general rise in import prices. Another reason is that in view of the need to assure regularity of supply (subject always to what I have already said of the relation between this security and the level of coal production) it may prove reasonable to retain sources whose costs do not allow them to be competitive. Such a policy, often pursued in the oil industry, can also be applied to coal, which is the chief form of domestic energy. Lastly, the coalfields certainly need time and relative security to continue the efforts at rationalization they have begun. To deny them this would be to jeopardize the entire process of rationalization.

So there are serious arguments for giving some security to the coal industry - within reasonable limits and until such time as nuclear energy can take over from traditional forms. The cost of such an operation would be by way of an insurance premium that the Community agreed to pay in order to have greater assurance of regular supplies, in so far as coal output slightly in excess of the level that would be strictly competitive could contribute to such assurance.

Naturally, whatever the output decided on, it should come only from the most productive pits, and some pressure should still be exerted on the coal industry to encourage it to continue and intensify the rationalization successfully undertaken some years ago.

However, ways and means of giving coal protection must be selected with care.

Protection in the forms now provided in all countries - quantitative restrictions, duties and taxes on consumption - has the effect of bringing the price of every kind of energy up to that of the most expensive.

It is evident that as the share of coal in the total supply of energy is dwindling steadily, there is less and less reason to maintain these forms of protection. Where as in 1950 coal met 70% of the Community's energy requirements, it accounted for no more than 52% in 1960 and will doubtless have dropped to 35% at most by 1970. During the same period, the share of petroleum rose from 10% in 1950 to 30% in 1960 and will probably be nearly 50% in 1970.

The justification for giving protection to coal being therefore political rather than economic - or, if you like, based on general economic policy - it would be logical for the burden to be carried by the economy as a whole and not only by the consumers of energy, as is the case at present.

The support that would thus be given to coal mining should not in the long run take the form of customs duties or quotas for coal or that of quotas for crude oil or heavy taxes on fuel oil; it should preferably be an aid to coal producers in the form of direct or indirect subsidies, for instance, which make it possible to pass smoothly from a protected market to a market more open to outside competition. It is up to the High Authority of ECSC to make the proposals which will embody these support measures in practical form.

As for petroloum, the Commission rocently agreed on the broad outline of the proposals it intonds to make to the Governments.

In presonting these proposals, the Commission is mindful of the experionce gained in the negotiations that lod oarly this year to acceptance of the common agricultural policy. The proposals constitute a common policy, each part of which may be the subject of separate negotiations (where the question has not already been settled by the Treaty of Romo) but which nevertheless must retain some overall cohesion on both the national and the Community planes.

In addition to the definition of common long-terms aims, which will be fully realized at the ond of the Common Market's transition period, these proposals contain temporary provisions which would enable existing national systems to morge smoothly into a Community system, while avoiding any repercussions that might damage either the economies of Member States or workers in particular.

For the final period, which should begin in 1970, the Commission proposes to set up a system incorporating the following provisions for petroloum: crude oil and petroloum products would circulate freely between Member States without restriction or customs duties, as laid down in the Treaty of Romo.

Imports of crude oil and petroloum products from non-member countries would be free, oexcept in the case of the Eastern bloc for which there would be a Community quota.

The common external tariff would remain zero for crude oil, and low duties would be applied to petroleum products; taxes on consumption which affect petroleum products for industrial use (mainly fuel oil) would be fixed at the lowest uniform rate for the whole Community (considerably below the rates currently charged in most Member States); the taxes on motor fuels would be brought into line, thus permitting the development of a satisfactory structure in the refinery industry.

Provision will be made for the effective diversification of sources of supply; this may include - although there are certain legal obstacles to the idea - complete or partial tax exemption for petroleum products derived from crude oil produced in the Community or in other areas whose output was to be encouraged.

With the same aim of assuring for the Community the greatest possible independence in its supplies, a common policy on stocks will be framed, fixing a minimum level for stocks and working out common methods of financing them.

The application of two different treaties to coal and to petroleum is an abnormal situation: different rules of competition are applied to the two products. To bring matters into line, a procedure will be devised to ensure that prices charged on the market in petroleum products are published after sales.

Finally, the oil companies will of course be subject to the rules of the Treaty of Rome, which are designed to prevent the abuse of dominant positions.

- 15 -

In view of the vital importance to the Community of regular and cheap supplies of energy, it seems indispensable that there should be a body whose duty it would be to watch over the application of the policy I have just outlined.

The Commission therefore intends to set up a standing committee, including representatives of the Member States and of the Commission, to keep an eye on both the movement of prices and the security of supplies in the oil market; it will also have to see to it that there is no overlapping in the construction of refineries and pipelines.

This is our goal. To get there, we shall have to define the stages by which national policies will gradually be harmonized and make way for action by the Community.

During this transition period, the first undertaking that governments must give is that they will neither enact new measures nor amend existing ones in any way which would make it more difficult to achieve the common policy which will be fixed for the period when the transition is completed. With this in mind, a procedure for prior consultation will have to be established, similar to that already arranged in other fields.

Transitional arrangements will be made for most of the aims assigned to the final period.

The movement of petroleum products within the Community is in the process of being freed. The Treaty of Rome clearly defines the stages by which customs duties are to be eliminated: on 1 July of this year,

account being taken of the speed-up decision recently reached, duties between Member States will only be half what they were before the Common Market was instituted.

The Treaty provides for a common customs tariff in trade with non-member countries. It has already been decided that crude oil shall be duty free. The duties for petroleum products still remain to be settled. The Commission, as directed by the Treaty, will no doubt make its proposals to the Member States in the course of this year; the lines laid down for energy policy imply that duties will be at a low level.

These provisions, however, do not yet apply to the Federal Republic, because she has the right - under the special protocol on mineral oils - to maintain until January 1964 the customs duties applied before the entry into force of the Treaty, i.e. DM 125 for a ton of crude oil and DM 129 for refined products. When the protocol expires, duties on imports from non-member countries will have to be aligned directly on the external tariff, while duties on imports from other Member States will be eliminated.

As for restrictions on trade between Member States, among the problems still to be solved is that of French controls. The EEC Commission has already sent the French Government its recommendations for increased import quotas. In any case, France must by the end of the transition period suppress all discrimination between the nationals of Member States in regard to conditions of supply or marketing of goods.

It is proposed to maintain freedom of imports from non-member countries, except for products from the Eastern bloc, for which a quota system is to be introduced. A Council decision in July 1961 established a procedure under which Member States would consult together before concluding commercial agreements; it is intended that from 1963 on there shall be a global quota divided among the Member States in the light of existing conditions and of any new needs that arise.

The other means of protection applied at present is the tax on consumption. The Treaty does not lay down any precise scheme for harmonizing these taxes, and it would not be impossible for each country to maintain its own set of taxes, all products being taxed by the country in which they are consumed, unlike taxes on production, which are refunded when goods are exported. However, because of the protective effect of these duties and their importance to user industries, the Commission considers that the taxes on energy products of concern to industry should gradually be harmonized, and it suggests that a very modest rate of tax should be envisaged for the end of the transition period. An intermediate stage at a higher level would be fixed for the beginning of the third stage on 1 January 1966.

Tax on motor fuels would gradually be harmonized in view of the effect the price of these fuels may have on the level of consumption and consequently on the structure of the refining industry.

Once the transition period is under way, the brunt of the work will fall on the Standing Committee on Petroleum Policy. The senior officials responsible for the oil sector in the Member States already meet regularly on the initiative of the Commission to keep

an eye on the situation. They have set up the machinery for exchanging information on investment in refineries, in transport and distribution, and in imports, particularly those from the Eastern bloc. These contacts will have to be amplified and extended to other aspects of the market, particularly to prices and the security of supplies.

Such, briefly, are the Commission's proposals. They are now being discussed with the High Authority of ECSC to make sure that they tie up with the arrangements envisaged for the coal market. They will then be communicated to the Governments and will form the basis of the coming discussions on energy policy.

°

°

°

Concluding their report, the Economic Research Institutes made the following remarks:

"If those responsible for economic policy believe that the German coalfields should continue to make a high contribution to total supplies, customs duties on coal imports will have to be maintained. Similarly, competition from fuel oil can only be restricted by means of a high tax on consumption. It is hardly necessary to point out that such measures can hardly be reconciled with the wish to let the consumer benefit by the cheapest sources of energy."

As you will have gathered from my remarks, the Commission has a very clear answer to this problem. The Commission believes that the Community must resolutely pursue a policy of cheap energy, while taking every precaution to ensure the necessary regularity in its supply of petroleum. Measures of support are certainly necessary for coal, and

the Community's coalfields cannot be left to face the danger of severe structural recessions.

But those measures of support must not inflate the price of cheap fuel to the detriment of the Community's industrial, agricultural and commercial activity as a whole, by aligning the price of industrial petroleum products on the cost of coal production, if for mainly social reasons it has been decided to keep these up.

o

o

o

Ladies and Gentlemen, these are our ideas on a common energy policy for the six countries of The Community. Of course, they constitute no more than a basis on which to work, for the proposals that the Inter-executive working Party is to make to the Governments will also have to incorporate the ideas of the High Authority and the Euratom Commission. But I think I may say, without too much fear of error, that the present situation on the energy market and foreseeable developments force us towards some such ideas as I have had the honour of explaining to you.