COMMISSION OF THE EUROPEAN COMMUNITIES

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DEVELOPMENTS IN THE REFINING SECTOR OF THE COMMUNITY OIL INDUSTRY

(Communication from the Commission to the Council)

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1. Introduction

As in the past the Commission has had a series of meetings with individual companies during which they provided details of their current policies, 1978 performance and 1979 forecasts. Although information was not provided by all companies, the information, on an overall Community basis, covers nearly 88% of probable crude runs.

The possible effects of the situation in Iran were not assessable at the time of these discussions and the following commentary is based on the assumption that overall disruption of supply will be minimal. Present uncertainty has, however, led to marked price increases in the Rotterdam spot market. This and the evident incentive to stock-build in anticipation of a January 1st OPEC price increase and perhaps as a hedge against the fluctuating dollar could easily lead to a considerable increase in the fourth quarter refinery throughput.

2. Industry Objectives for 1978

Early in the year it appeared, from the sum of the many different company plans, that for the Community as a whole, refinery runs would be less than 0.5% higher than actual performance in 1977. During the early months many companies made further reductions to their objectives and by May/June it appeared that 1978 throughput would be below 1977 levels.

Industry did expect a growth in demand, but only a small one of less than 2%, above the 527 million ton consumption level of 1977, and planned to meet requirements not covered by refinery runs by purchases on the spot market and the reduction of stocks from the abnormally high level that they had reached by the end of 1977.

3. Actual 1978 performance

Latest estimates show that in many cases, runs were increased over the originally planned levels. For the Community as a whole, 1978 throughput

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is now expected to be 1% above 1977 levels when 531 million tons were processed.[1] This increases the rate of utilisation of capacity in service to a level approaching 70% (this represents 64% use of the 844 million tons of 1978 installed capacity). This Community average figure does not adequately illustrate that in some Member States, notably Italy, there is a concentration of surplus capacity and utilisation is much lower than Community average.

This increase of utilisation rate has proved possible without the generation of surpluses damaging to the industry and to a large degree yields have been balanced by purchases and stock reductions.

Overall, the figures suggest an unexpected increase in demand near the end of the year. While industry are not yet able to fully analyse the underlying market developments it appears most likely that the increase in demand, mostly for middle distillates, is not directly related to increased consumption but that, at consumer level, feelings of insecurity about future price and tax levels have motivated considerable consumer stock building. Overall, there has been a much better balance between supply and demand than in 1977.

4. Industry Objectives for 1979

Although as always there is considerable variation between individual company plans, the overall Community position shows an increase in refinery runs of about 3.75%. It should be noted that this exceeds the generally forecast demand growth of about 2%-2½%. Thus it is clear that the reasonable balance between supply and demand that was maintained in 1978 could, in 1979, be threatened by a return to over-production in terms of refinery output. This situation results from increased throughput plans on the part of some, but by no means all companies. Several companies forecast lower levels for 1979. Initially, increases may be held back by physical lack of incremental crude supply but, over the year, companies now planning to increase runs may be dissuaded by the risk that surpluses will undermine market prices. This delicate situation needs to be kept under review.

5. Imports

There is no discernible trend towards an increase in imports which fluctuate on a normal commercial basis. In 1978 some 5 million tons of net imports contributed to Community supply whereas in 1979 imports and exports are expected to cancel out.

(1) Reference 22nd May 1978 Communication from the Commission services "The Balance and Structure of Refining within the Community"

For the longer term analysis of the import situation the Commission has set up and had two meetings of a working party of experts from Member States. A report will be made to the Energy Committee.

6. Distillation Capacity

Based on information obtained from the companies there have been no proposals for new projects and the situation remains as presented in March 1977[1]. Thus further growth in the sector appears unlikely at present. Final confirmation of the investment position will be provided by information made available under Regulation 1056 at the beginning of 1979 and a subsequent report will be made on this subject.

7. Cracking Capacity

Since January 1977 the conversion capacity installed in Community refineries has been increased by nearly 14 million tons/year. The largest part of this (8.2 m.t/y) is in the form of "visbreaking" units which lighten fuel oil and increase the yield of middle distillates. Many of these new visbreakers are converted crude distillation units and thus in addition to increasing conversion capacity their change of function provides a much needed reduction of distillation capacity. Currently constructed and planned conversion capacity appears adequate to meet future needs and there would appear to be no justification for Community action in this sector.

8. Plant Closure

Despite some minor closures not foreseen in May, surplus distillation capacity within the Community remains a serious problem. Although, on present estimates, it appears that there is still a need to close 70 million tons of distillation capacity, this figure must be viewed with some reserve especially since a major part of reductions made so far have been achieved only by the temporary withdrawal of units from service. These units still exist and could be brought back into operation. Apart from this qualification of the reductions so far made, it must also be recognised that the industry has probably reached the limit of reductions that can be made by the closure of individual distillation units within refineries that continue to operate. The further reductions that are still necessary will

[1] "Community approach to the refining problems of the Community" (COM(78)71 final)

inevitably involve the closure of whole refineries. As has been all too painfully demonstrated in the few cases where this has already happened, refinery closure leads to social and employment problems. In view of the inevitability of further closures, the Commission has, for some time now, considered that aid at Community level is necessary to help in the solution of these problems.

9. Resume

- In 1978 refinery throughput rose above estimates but will finally show little more than 1% growth over 1977.
- Because of this limited growth and prudent product purchases by most companies, a well balanced supply/demand situation has been maintained in 1978.
- 1979 refinery programmes are, in aggregate, on the high side compared to anticipated demand. Careful management is going to be necessary to maintain a proper balance and avoid the weakening of market prices that can be created by surpluses.
- Imports are stable except for normal commercial fluctuations.
- There are no new plans to increase distillation capacity.
- Cracking capacity in the years ahead appears likely to be adequate.
- Distillation plant closure is still necessary and, since in future this is likely to be achieved only through whole refinery closure, problems must be anticipated.

10. Conclusion

Since the last communication there has been a reasonable improvement in the refining sector. This has been due in part to permanent and temporary plant closure and also to an increased awareness on the part of industry leading to notable self-restraint in the disposal of surplus product into the spot market.

It must however be recognised that the bases for these improvements are not sufficiently firm to allow complacency. Plans for 1979 already suggest that balance may be destroyed. Consequently the Commission proposes to continue to obtain information from the refining sector and keep developments under review and will report to the Council when necessary.

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Only further permanent closures will provide better stability and assistance should be given to the overcoming of the problems associated with refinery closures. If refinery closure has particularly grave structural consequences in some regions or zones of the Community, actions must be foreseen to provide alternative job opportunities for workers made redundant.

In this context, attention has been drawn on earlier occasions[1] to the possibility, if need be, of providing Community finance by, for example, grants under the Regional Development Fund.

Alternatively, it should be recalled that aid might be envisaged in the context of general industrial restructuring, for which a proposal has already been submitted to the Council[2] and which should be employed in the refining sector. For this purpose the Commission has already proposed that 10 million u.a. should be made available (for this a P.M. entry has been made in the 1979 budget) and intends to propose such subsequent funds as may prove necessary on a yearly basis.

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(1)(Document COM (78) 71 final dated 22 February 1978)

(2)(Document COM (78) 532 final dated 26 October 1978)