SK EU2016
Slovak Presidency of the Council of the European Union

Energy Prices and Costs in context of the EU Competitiveness

Discussion paper for the Informal Meeting of the EU Energy Ministers
Bratislava, 13 July 2016

One of the goals of the Energy Union is to achieve EU climate and energy objectives at affordable costs for households and industries. The Energy Union's vision is to have strong, innovative and competitive European companies that develop the industrial products and technology needed to deliver energy-efficient and low-carbon technologies inside and outside Europe and to reduce consumers´ energy bills. Investment confidence should be enhanced by stable price signals.

To address the energy price challenge, in January 2014 the Commission undertook its first major assessment of energy prices and costs and issued the Communication on Energy Prices and Costs in Europe. It found that there were major differences in industry electricity and gas prices between Member States, and that EU prices overall were often higher than those of major trading partners, specifically twice and four times as high as those in the USA. The Communication concluded that further efforts were needed to create the internal electricity and gas markets and to ensure that energy and climate policy objectives are achieved as cost effectively as possible. In particular, energy efficiency measures need to be enhanced and internal market distortions and barriers to the free flow of energy need to be removed. Such efforts could improve the efficiency of energy markets and reduce prices, and increase energy savings to further reduce costs.

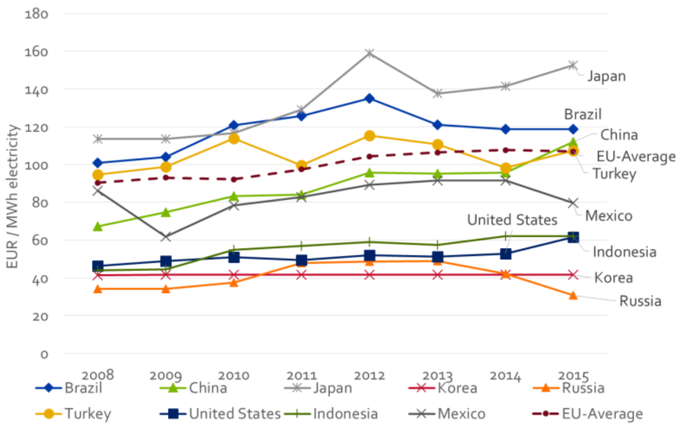
Building on the Commission Communication, the Council adopted conclusions on energy prices and costs, the protection of vulnerable consumers and competitiveness in June 2014. These stressed that, to maintain competitiveness of the European industry, the EU should mitigate energy cost differentials with competitors and support innovation and investments in energy efficiency. As part of the Energy Union Framework Strategy the Commission subsequently committed to producing further reports on energy prices and costs and adopted a legislative proposal to improve the detail and transparency of energy price statistics. This proposal is currently in the ordinary legislative procedure.[1]

In 2014 and 2015, we witnessed a dramatic decrease in wholesale energy prices, oil in particular. EU wholesale electricity prices are at their lowest for 12 years, wholesale gas prices have fallen by 50% since 2013, and wholesale petrol prices by 77% in the last 19 months.[2] Although prices decreased globally, the EU´s position as regards the main trading regions has not changed significantly; furthermore, the price reductions have not always been passed on to final consumers. Whilst retail petrol prices have fallen 24% since June 2014[3], retail electricity prices have increased by around 3% a year since 2008 and gas prices by 2%. One reason for this is that the energy component of the retail price has diminished while network costs, levies and taxes as a proportion of the final price have increased. A better understanding of the main drivers behind these increases would contribute to the better informed political decision-making needed to achieve EU energy and climate objectives. In addition, there are still significant differences in prices across Member States, driven by insufficient liquidity of the market due to the lack of integration

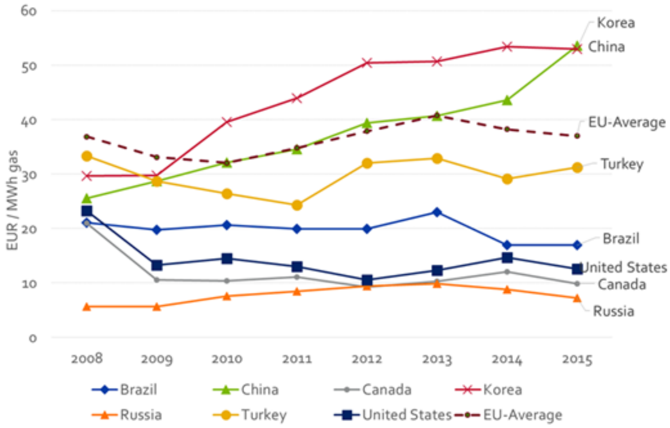
[1] Proposal for a Regulation of the European Parliament and of the Council on European statistics on natural gas and electricity prices, repealing Directive 2008/92/EC.
[2] The ITRE report Recent Trends in Energy Prices (2015). Analysis revealed that 2014 to 2015, average petrol prices excluding taxes decreased by 27%, but the average pump price decreased only by 9%, due to the increased tax component. Similar results occurred with diesel. In 2014 to 2015, electricity prices, excluding taxes, decreased by 4.5%, but the final domestic electricity price for medium consumers increased by 1.8 %. Similarly, the fall in wholesale prices of natural gas has been mitigated at retail level.
[3] to February 2016, based on the European Commission´s findings.

between respective regional markets, the absence of cross-border infrastructure and the existence of different tax, levy and state aid regimes.

Electricity prices



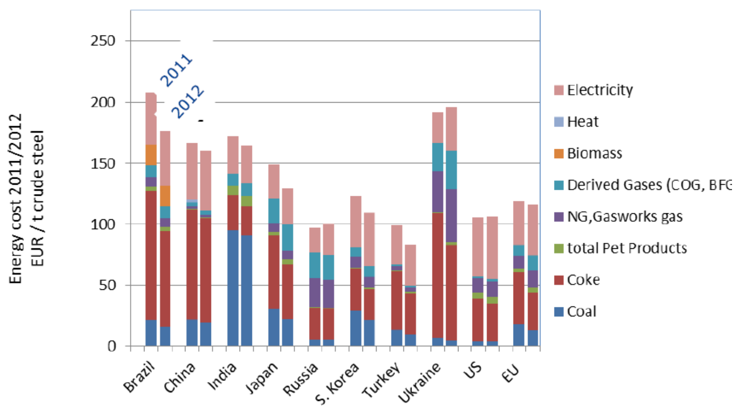
Gas prices



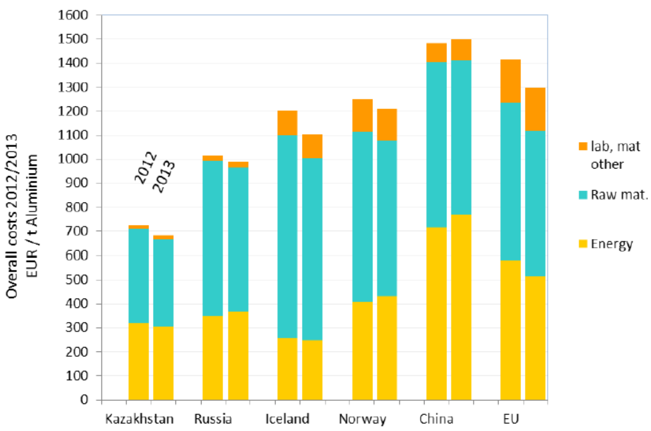
Source: European Commission´s findings.

Energy price levels for industry in the EU still remain well above the levels in the USA or Russia, even if EU energy prices are mostly lower than those in Asia. Prices in the EU should be considered in conjunction with European industry's energy consumption, which is more efficient than in many other parts of the world. Overall, energy costs comprise less than 2% of European businesses' production costs. Nevertheless, it must be noted that energy costs can constitute a considerable proportion of the production costs of energy-intensive industries, particularly petroleum refining, iron and steel, chemical, petrochemical or aluminium production, as illustrated by the examples below. Given the interdependence of primary industrial production and other sectors of the national economy, energy price levels and costs are of the utmost importance for EU competitiveness.

Iron & Steel



Aluminium



Source: JRC Report Production costs from energy-intensive industries in the EU and third countries, 2016

Fluctuations in energy prices and the availability of energy sources such as natural gas considerably affect those sectors facing strong international competition. Therefore a range of instruments exist in the EU to protect vulnerable energy-intensive industries from major price differentials; a range of tax exemptions, levy exemptions (such as free ETS allowances), tariff exemptions and other subsidies exist to mitigate risks of carbon and investment leakage or other consequences of international competition with potential negative impacts on the economy and environment. These measures, however, are as such not sufficient to create a level playing field for these industries. This was recognized at the meetings of the High Level Expert Group on Energy-Intensive Industries in December 2015 and June 2016. There the stakeholders expressed their view that the EU should urgently deal with the issue of high energy costs, the predictability and stability of the investment environment, the reform of the EU ETS and the need to stop investment outflow from the EU by supporting research, innovation and development.

In the aftermath of the global financial crisis and through a wide range of energy efficiency measures, the EU has taken steps towards decoupling energy consumption from economic growth and thus decreasing further the burden of energy costs on the economy. Despite such a positive recent trend, the EU's position compared with major trading regions has not changed significantly and therefore exposure to global price fluctuations and competition still raises concerns for Europe's international competitiveness. The energy transition (with more decarbonised and distributed generation and smart consumption), maintaining security of electricity, gas and oil supplies and building the infrastructure for the internal market may all have an impact on energy prices in Europe.

To this end, the Slovak Presidency of the Council of the European Union proposes to table the following questions for discussion at the Informal Meeting of the EU Energy Ministers:

1. **Are the different recent trends in energy prices underpinned by market fundamentals or are policy, regulatory/legislative or fiscal measures more significant in determining energy prices?**

2. **How can we ensure such an approach to achieving the EU energy and climate objectives, one which provides price signals for the energy market and consumers while taking into account the impact of different policies on energy prices and costs for EU industry and households? Are there any more specific measures which should be considered to help decrease energy prices and costs and the burden on EU business?**

Kindly note that contributions will be strictly limited to 3 minutes per delegation. We invite Ministers to focus on their top priorities; we welcome receiving in writing any additional comments they may have.