STATEMENT OF THE FEDERATION OF ALUMINIUM CONSUMERS IN EUROPE

URGENT NEED FOR THE TOTAL SUSPENSION (0%) OF THE EU TARIFFS ON PRIMARY ALUMINIUM

Since the Council Regulation (Taxud/944/2006 – COM (2006) XXX) of 17.10.2006 suspending the autonomous common customs tariff duty for not-alloyed primary aluminium (current rate: 3%), <u>the situation of the EU downstream aluminium industry continues to worsen.</u>

The recent reduction from 6% to 3% in the tariff of not-alloyed aluminium has brought some benefits to some downstream companies in the EU, but this is not sufficient to redress the situation, nor will it allow the EU non integrated transformers and final users to compete effectively both within the EU and in foreign markets.

The existence of a 3% duty on primary non alloyed aluminium and of a 6% duty on alloyed primary aluminium continues to create *de facto* severe market distortions and the competitive disadvantages of the independents aluminium transformers and final users on downstream product markets.

This situation puts at risk the only segment of the EU aluminium industry that could create jobs.

<u>It requires the remedy of a total suspension on all headings for primary aluminium,</u> taking into account the new structure of the EU aluminium industry, the foreseeable evolution, the negative effects of the duties still applying on diverse forms of primary aluminium and the threat to the very survival of essential segments of this industry in Europe.

Moreover, this request is completely coherent with the Competitiveness Council conclusions entitled:
"A Fresh Impetus for Competitiveness and Innovation of the European Economy"
as adopted uninamously at the meeting of 29 -30 May 2008, where in point 3.2
<u>concerning competitiveness in metals industries and forest-based industries,</u>
the Council «…….invites the Commission to put in practice all the actions to encourage a sustainable supply of strategic materials to the metals-industries …….. <u>including through promotion of recycling, eliminating distortions in trade, namely through endeavouring to remove all tariff and non-tariff barriers….».</u>

I. The new situation in the EU aluminium industry

The Rio Tinto/Alcan merger has initiated a new wave of restructurations in the aluminium industry. This trend is confirmed by the bid of BHP Billiton on RTZ/Alcan and by the

intervention of Chinese players into the battle, not to mention the potential moves around Alcoa.
The aluminium industry is realigning upstream.
We see a new scenario based on the interests of mining giants integrating the mining of bauxite, its refining into alumina and the smelting of aluminium.

As a consequence, the traditional integrated groups are disinvesting from their downstream businesses.

A few years ago, EU independent aluminium transformers represented around 50% of the workforce of the EU aluminium industry. With the forming of Aleris and of Novelis as the result of the disinvestment of downstream assets by the traditional integrated groups, inter alia, **today independent aluminium transformers form around 95% of the EU aluminium industry workforce.**

The EU aluminium market is currently divided between:

1) an oligopolistic group of 3 major integrated producers (RTZ/Alcan, Alcoa, Hydro) who accounts for around 5% of the EU aluminium workforce. They constantly cut jobs and they are now integrating upstream with mining giants, while disinvesting downstream businesses.

   These groups want to retain tariffs on primary aluminium because the inclusion of the equivalent of the value of the duty in the market premiums for all kinds of primary aluminium sold in the EU brings to them extra- revenues.

   This mechanism has been continuously denounced by FACE, the Federation of Aluminium Consumers in Europe, as a « hidden subsidy »;

2) thousands of SME's and some major groups such as Aleris and Novelis, that constitutes now more or less 95% of the EU aluminium industry workforce.

   This sector is the future of the EU aluminium industry, as smelting capacities will continue to reduce in Europe while the consumption of aluminium products will continue to grow at an estimated pace of 4% annually.

   However, the existence of a 6% duty on alloyed primary aluminium and of a 3% duty on not-alloyed primary aluminium severely affects the domestic and international competitiveness of the EU independent aluminium transformers.

   It creates a physical barrier that makes it more difficult and costly for them to source stable, sufficient and competitive supplies of metal.

   It creates market distortions, to the point that, in a speech in Stockholm on the relations between trade policy and competitiveness, the EU Trade Commissioner, Mr Peter Mandelson, described the EU aluminium market as a **« pocket of distortion ».**

Moreover, the general artificial inclusion of an equivalent to the value of the duties in the sales price for aluminium in the EU, irrespectively of its origin (duty-free/dutiable), costs unnecessarily around 500 million euros more annually to EU aluminium transformers and consumers.

This amount is cashed as a « hidden subsidy » essentially by the integrated producers such as Hydro, RTZ-Alcan, Alcoa, BHP-Billiton and by smelters based in non-EU countries enjoying duty-free status for primary aluminium (most of them belonging to the same integrated groups who therefore control the so-called "duty free" supplies to the EU).

The new structure of the EU aluminium industry and the magnitude of the adverse consequences of the current EU aluminium tariffs impose the urgent total suspension (0%) of the duty on all the types of primary aluminium .

II. Foreseeable evolution of the flows of primary aluminium*

In the EU, the total primary capacity (primary metal capacity at the reduction section of smelters, before any remelting of scrap or purchased ingot from other plants to produce additional primary ingot products) of the EU 27 is 3.19 million tpy, while the reported capacity for secondary aluminium (metal produced by recycling external scrap, before any addition of purchased ingot from other plants) is 4.07 million tonnes.

The combined capacity of metal consuming plants at full capacity is such that, after allowing for the use of external scrap to meet part of the requirements at rolling and extrusion plants, **the EU 27 has a net deficit of 5.02 million tonnes of aluminium ingot products.**
These must be imported from outside the EU 27. This figure of 5.02m tonnes compares with the reported net imports of unwrought aluminium into the EU 27 in 2006 of 4.86m tonnes.
The same analysis applies to the companies with the largest net purchase of ingot products in the EU 27, who are shown in the table below:

EU 27: Largest Net Purchasers
(000 tonnes)

Origin	*Base*	*Net Purchse*
Birla Hindalco Group	India	1112
Hydro Aluminium Group	Norway	414
Aleris Group	USA	396
Elkem Group	Norway	373
Alcoa Group	USA	273
Viohalco Group	Greece	237
Others		2216
Total		***5021***

Birla Hindalco Group acquired the aluminium rolling plants of Novelis (formerly Alcan). Birla has aluminium smelting capacity in India, but this is used for the domestic market. Metal for its plants in the EU must be purchased from third parties.
Hydro Aluminium's metal requirements exceed the capacity of its smelters and affiliates in Germany, Slovenia and Slovakia. These can be met by duty-free imports from its smelting capacity in Norway.

**Primary aluminium here includes all the forms of primary metal. Please see attached the study on "Primary Aluminium Flows" by James King, senior metals economist.*

Aleris Group acquired the rolling mills of Corus. The company has capacity for secondary ingot products in the EU 27, but no capacity for primary ingot products to supply those rolling mills.
Elkem Group can meet most of its requirements by duty-free imports from its primary smelting capacity in Norway.
Alcoa Group has primary smelting capacity in Italy and Spain, which are exceeded by its metal requirements. These can be met by duty-free imports from smelting capacity in Norway, Ghana and (from 2007) Iceland.
Viohalco Group has no smelting capacity and must purchase from third parties.

This is to say that the big producers who are making pressures to maintain EU import duties on primary aluminium are themselves hugely in deficit and net purchasers for the same primary aluminium.

This clearly demonstrates that keeping the duties is motivated by their desire to continue to benefit from the "hidden subsidy" effect of the tariff. In doing so they continue to gain unfair competitive advantages over the EU independent aluminium transformers, to collectively increase the EU market premiums in an artificial way so that non-EU potential suppliers of primary metal are kept away from a completely untransparent and distorted European aluminium market.

EU 27: Net Position by Product
(000 tonnes)

Origin	*Net Position*
remelt ingot	-3509
slab	-464
billet	-1967
primary foundry alloy	222
secondary foundry alloy	515
others	182
Total	***-5021***

The structural shortage of primary aluminium in the European Union will become a major issue and a growing challenge for European producers of semi-fabricated products and alloys. This situation is set to worsen as signs of global western world shortages are mounting, aggravated by the rise of demand in China, India and other emerging markets.

In the context of growing demand and of maintained European import tariffs, major aluminium producers (the Gulf, Brazil and Russia, for example), may find better margins in other locations, creating additional difficulties for European transformers.

The recent shutdown of aluminium capacities in China due to weather storms, toughened environmental legislation and the raise of prices on oil and coal (a major source of energy in

China) may turn China into a new importer, changing the primary aluminium flows dramatically to the detriment of the EU if the tariffs are not totally suspended.

This along with other global developments will worsen the shortage of primary aluminium in Europe and will increase pricing speculations.

Despite the economic slowdown, the consumption of aluminium in the EU is expected to increase to 7.4 million tonnes in 2008, and will further increase up to 8 million tonnes by 2012 with an average annual growth of 4%.

At the same time the production of primary aluminium is expected to decrease gradually from 3.1 million tonnes in 2007 down to 2.86 million tonnes by 2012.

As the remaining European producers will have to rely even more heavily than now on imports of primary aluminium, there is no guarantee that sufficient, predictable and competitive supplies will be available to European transformers.

The net imports of the EU are forecasted to rise to about 5 million tonnes by 2010 and close to 7 million tonnes by 2020.

After 2015 net imports will represent 70% of the European Union consumption of primary aluminium.

In this context it has to be stressed that in 2006 the gap between the quantities potentially available from duty-free origins and the import requirements of the EU was 1,6 million tonnes.

Even with assumptions of new smelter capacity for export in currently duty free origins, the gap is forecast to increase sharply by 2015 and to be close to a 3 million tonnes in 2025.

However it must be noted that there is no duty-free priced primary aluminium available in the EU market, because of the generalised practice to include an equivalent of the value of the duty as an extra premium for all the primary aluminium sold in Europe, even when this metal has been smelted in the EU or imported from a duty-free origin. The duties push artificially the whole pricing structure to the top, making primary aluminium more expensive in the EU than elsewhere.

III. Competition concerns

The aluminium market in the EU is deeply divided between, on the one hand, three non-EU owned multinational groups that constitute the Traditional Suppliers, and on the other hand numerous, largely small, downstream suppliers that are reliant on aluminium from smelters, namely the EU Transformers. The Traditional Suppliers are mainly Alcan (Canada), Alcoa (USA) and Hydro (Norway).
The EU market for aluminium is to a wide extent dominated by the Traditional Suppliers, which are located outside the EU and are fully integrated entities from mining to end processing interests. This has lead to the situation that the EU Transformers, which are largely SME's in the EU using aluminium for industrial transformation, have little access to Community produced or duty free imports of such products, with the result that those companies risk to become uncompetitive due to the payment of import duties.

Approximately less than one third of imports are subject to the tariffs. However, the Traditional Suppliers represent the vast majority of importers of the duty free product. Consequently, the EU Transformers' primary available sources for imported aluminium are largely subject to tariffs. As the Commission has previously identified when referring to the manufacturing plants of not-alloyed aluminium in the EU *"almost all these plants belong ...to major industrial holdings located outside the European Union [in other words the Traditional Suppliers]. The aluminium produced in these plants and supplied duty free is mainly used for further transformation within companies linked to these holdings."* (Council Regulation (EC) No 501/2007, OJL 119/1, preamble 4.)
There is a strongly held view by the EU Transformers that the Traditional Suppliers have an inherent desire to continue to have the tariffs imposed by the EU because it protects them from competition from the EU Transformers, and from non-EU based primary aluminium suppliers, through raising the cost of aluminium to EU Transformers.
The Traditional Suppliers are the principal actors behind the complaints and lobbying that occur in relation to the continued maintenance of the tariffs. There is a strongly held view by the EU Transformers that the Traditional Suppliers and those with similar interests (traders) have acted in a coordinated manner to ensure that the EU Transformers are not successful in having the tariffs removed. This activity artificially prolongs the life of the market distortions created by the tariff and this is for the benefit of these suppliers. In the view of the EU Transformers, this activity is anticompetitive and a breach of the EU Treaty articles on competition. The 2007 *AstraZeneca* case may by analogy be relevant. In that case AstraZeneca was held by the European Commission to have misused patent rules and procedures and to have supplied to the patent authorities misleading information in relation to a drug. The European Commission found that AstraZeneca held a dominant position in relation to that drug and that its conduct was an abuse of that dominant position. The EU Transformers consider the Traditional Suppliers and those with a similar interest have 'gamed' the trade tariff system to their benefit and that this conduct should be dealt with by the competition authorities in a similar way to the treatment of AstraZeneca. Furthermore, the EU Transformers consider that around the core activity of initiation and maintenance, through lobbying, of the tariffs, the Traditional Suppliers have conducted themselves such that there has been and continues to be a negative competitive effect, and this should be investigated by the competition authorities.

IV. The distortions of the market and the need of a full suspension of the tariff on all the forms of primary aluminium

The acquisition of Alcan by RTZ reduces further the EU based smelters supplying European independent customers.
The declared strategy of RTZ and Alcan management to further divest downstream assets, in view of reducing the RTZ borrowing to purchase Alcan, will put more European downstream companies under pressure to reduce costs and to cut their workforce because of the global competition.

The duty reduction to 3% on unalloyed ingot has benefited some companies, but put many others at further disadvantage as premiums for duty paid primary alloyed products such as billets, slabs and foundry alloys for wheels moved further out of line with competitive world markets.

Over recent months European market premiums for billets have been in a range between \$450-490. US premiums for billets delivered to customers on similar terms has been in the range between \$240-285. Asian premiums including Japan and Korea have been in the range

$220-240. Premiums for foundry alloys for wheels have been between $355-390 in Europe, with US premiums around $220-240 and Asia at $175-195.

<u>European downstream consumers are at a disadvantage of around $150-200 per tonne in an increasingly competitive world.</u>

The majority of European aluminium smelters are now owned by international companies RTZ-Alcan, Alcoa and Hydro, most of whose strategic investment interests are outside the EU.

The EU downstream aluminium industry which employs around 95% of the workforce is continuously moving into the independent market as the process of divestment gathers pace.

<u>These independent downstream companies are the ones who can protect and even grow employment, but only if they are on a level playing field on raw materials costs. Removing the duty on alloyed an not-alloyed primary aluminium is the only way to do it.</u>

Moreover, due to the permanence of 3% duty on not-alloyed primary aluminium and of a 6% duty on alloyed primary aluminium, the EU continues to keep off market flows of primary metal that could be sourced for example from Russia or from the Gulf.

This situation, besides encouraging market distortions and speculative pricing behaviours, has two other consequences:

1. European independent transformers have more limited capacity to obtain sufficient, stable and competitive supplies of the high quality primary aluminium under the form of billets or rolling slabs that they need to manufacture high added value products.

2. Millions of tonnes of remelt ingots are converted into extrusion billets or rolling slabs or foundry alloys by some primary producers in the EU. These remelting operations are avoidable and they take place only because of the distortions created by the presence of the duty; in fact, these primary producers have studied a stratagem, and they, apart from the usual production of formats transformed directly from liquid metal from their smelters, remelt millions of tons of aluminium supplied externally to produce extra quantities of billets or rolling slabs or foundry alloys. The practice of utilising remelting to produce foundry alloys, billets or rolling slabs is a virtuous mechanism, and it is largely adopted by non integrated European transformers to compensate for the EU primary metal deficit through the recovery and recycling of scraps, opportunely integrated by pure primary. But this mechanism when put into practice by some primary producers to make a further profit on the price differential tied to the duty (for example 3% on not alloyed primary metal and 6% on alloyed primary metal), represents an economic non sense for the industrial system in that it leads to extra remelting carried out purely to make a profit on the current duty differentials (creating a phenomenon of even further distortions and speculations) and not for reutilizing recyclable material (as is the case of the non integrated remelters, often related to transformation plants). This same mechanism is accompanied by additional energy consumption and useless carbon emissions.

V. Conclusions

Market trends, distortions of competition, competitive weakening of the EU downstream aluminium sector, new mergers in the pipeline, growing competition of products from third countries, excessively high premiums for aluminium and environmental concerns, all together make it urgent and vital to totally suspend (0%) the EU tariffs on all the forms of primary aluminium.

The subsequent creation of a fair level playing-field would improve the competitiveness of the European aluminium industry, would support the growth of demand for an environment friendly metal aluminium and would contribute to save or create thousands of jobs in the EU.

As it has been widely reported in major EU media, in exchange of the maintaining of the "protection" of the duties on primary aluminium, the major integrated producers have "rewarded" the EU Commission and the EU Member States with continuous massive job cuts in Europe, and with the decrease of technology investments in the downstream sector, contrary to the merger's committements made by them to the EU Competition Authorities.

In line with the objectives of the Jobs and Growth policy and of the Lisbon Strategy, it is time now for the EU leadership to act urgently with a sense of responsibility towards the thousands of SME's who represent the future of the EU aluminium system and who, according to the EU industrial policy, should be supported by totally suspending (0%) the EU duties on primary aluminium.

Brescia 17/07/2008

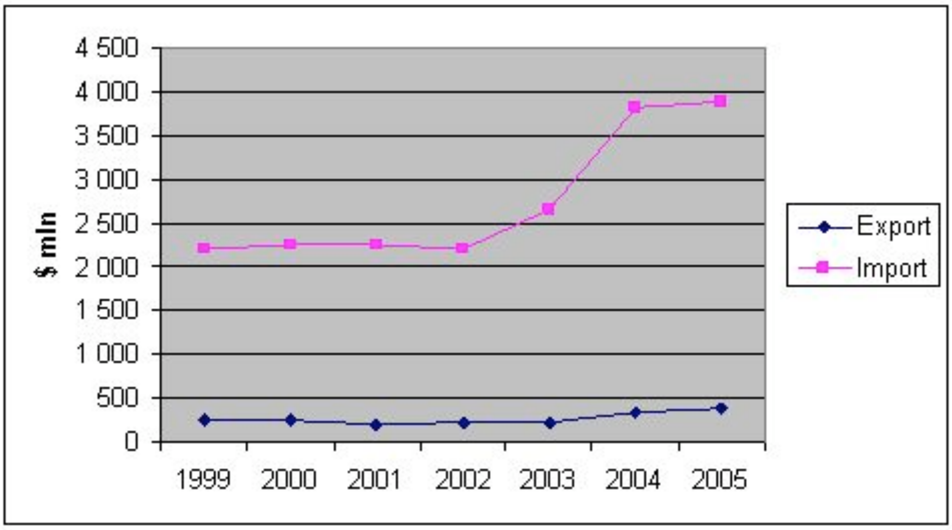
ANNEXES

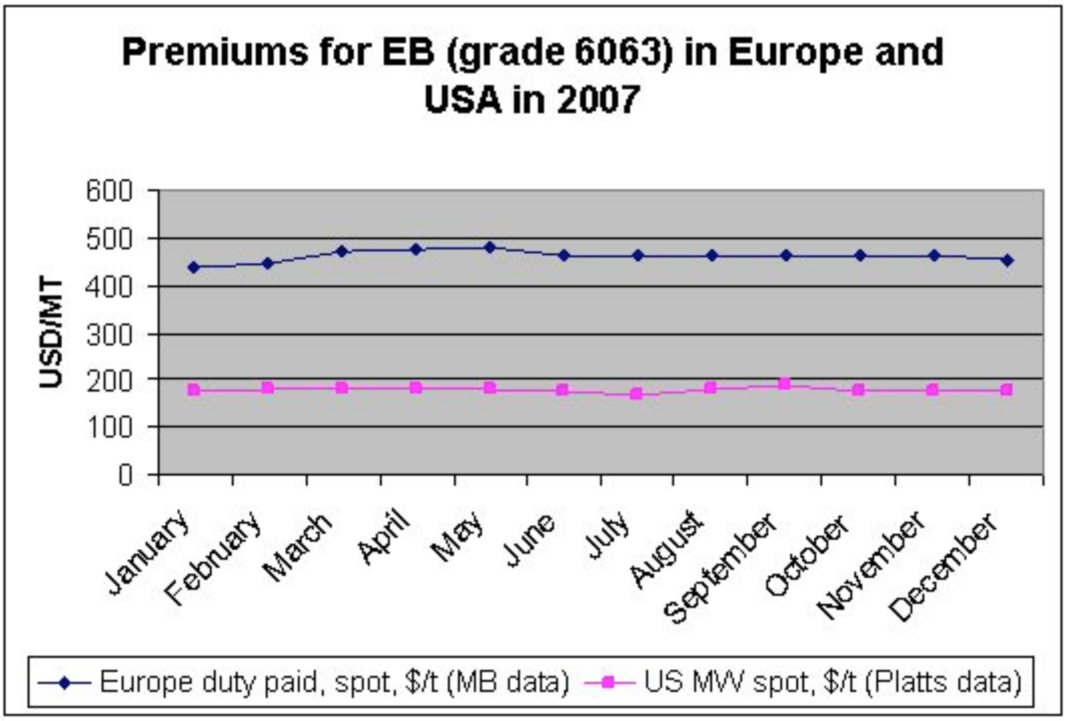
Annex 1: graphs on this and on the next pages.

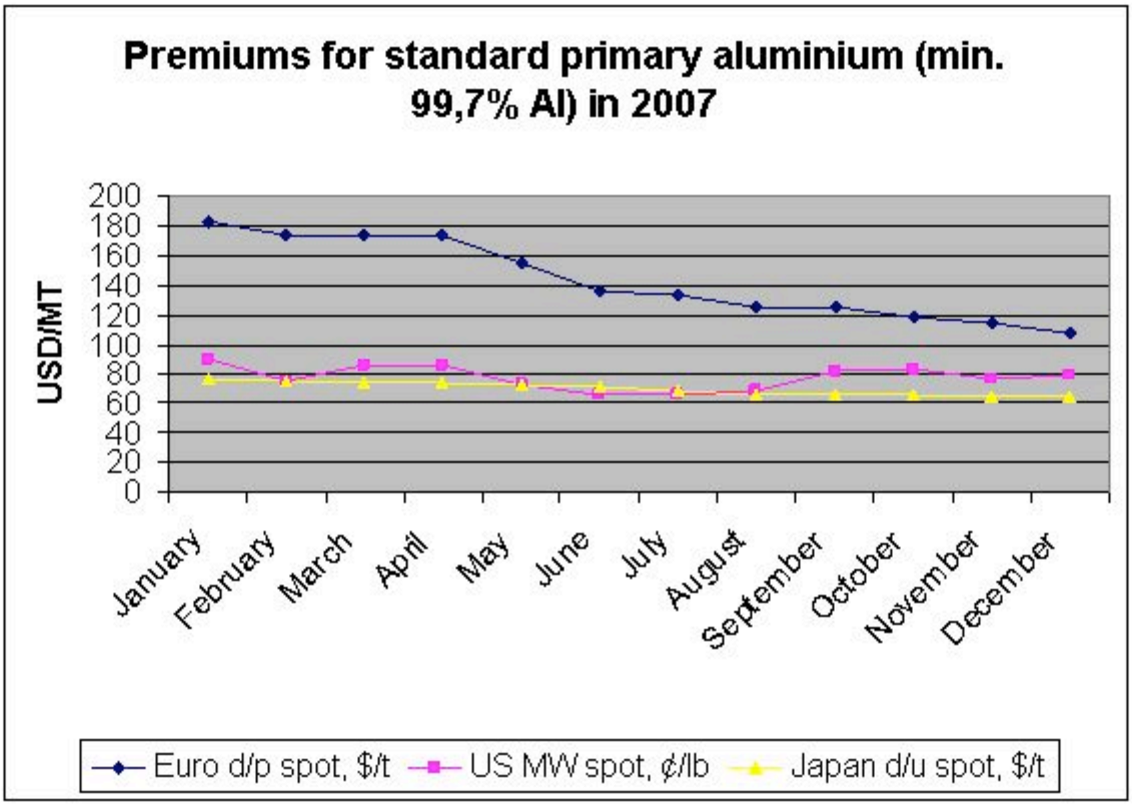
Annex 2: Statement of FACE on competition concerns raised by the duties on primary aluminium.

Annex 3: study on **"PRIMARY ALUMINIUM FLOWS"** made by James King, January 2008 (as attachment).

EU – 25 export/import of aluminium alloys in 1999-2005 ($mln, data from UN website)




Premiums for EB (grade 6063) in Europe and USA in 2007
USD/MT
600
500
400
300
200
100
0
January
February
March
April
May
June
July
August
September
October
November
December
Europe duty paid, spot, $/t (MB data)
US MW spot, $/t (Platts data)



Premiums for standard primary aluminium (min. 99,7% Al) in 2007
USD/MT
200
180
160
140
120
100
80
60
40
20
0
January
February
March
April
May
June
July
August
September
October
November
December
Euro d/p spot, $/t
US MW spot, ¢/lb
Japan d/u spot, $/t