European Aluminium recommendations on the EU response to the US Inflation Reduction Act

Brussels, January 2023

European Aluminium, the industry association representing the whole aluminium value chain in Europe, believes that now more than ever, it is time for the EU to ensure that the European Green Deal provides effective measures to incentivise European industries to keep operating and thriving in Europe and globally. Those European industries that are key for the energy transition must be provided with the framework conditions and the support needed to keep their businesses running and avoid further deterioration of their competitiveness, especially now that other leading economies are taking actions to attract investments in green technologies and provide competitive advantages for industries, such as the US Inflation Reduction Act (IRA).

The aluminium industry is one of those essential industries Europe cannot afford to lose; aluminium is used in almost all energy generation, transmission, and storage technologies: from solar renewable power to alternative fuel cells and hydrogen production to high-voltage cables and batteries, being indispensable for the transition towards a green European economy. As demonstrated by a study by KU Leuven, the EU energy transition alone will lead to a 30% increase in aluminium demand by 2040 with electric vehicles, solar power, and electricity networks as the main growth drivers. Europe will need aluminium in greater quantities than today, but there is a risk for the complete outsource of aluminium manufacturing, causing a strategic dependency of the supply, if no policy actions are taken in the short and medium terms. Instead, Europe should aim at maintaining and even increasing its share in meeting the rising domestic and global demand for aluminium.

In response to the US Inflation Reduction Act (IRA), European Aluminium has identified a series of measures for the consideration of EU policymakers, which would benefit not only the aluminium industry but the overall EU economy, while driving decarbonisation.

The EU must work on a long-term industrial strategy

The development at EU level of a consistent and effective industrial strategy that goes beyond mere crisis management and that reverses the trend of deindustrialisation has become today, more than ever, the essential condition for industry's survival in Europe. Supporting sustainable growth and the European industrial efforts to decarbonise their operations with concrete and effective measures, ensuring access to affordable decarbonised energy sources, should be at the core of a revised EU industrial strategy.

Learning from the US IRA, which provides some attractive measures for companies contributing to the shift towards a fully decarbonised economy, such as tax credits for certain investments, the new EU industrial strategy should also look at ways to incentivise EU green technologies production.

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ANYTHING BUT BASIC

Differently from existing European measures, the IRA provides a pragmatic and simplified taxonomy in certain areas that will accelerate the development of greenfield projects while leaving the market to promote technological solutions. One example is the clear link of subsidies to CO2 emissions – the lower carbon footprint, the higher subsidies (e.g. automatic tax credits for 10 years).

The EU should promote an equivalent "European Investment Act", which would incentivise the production of key technologies in Europe, using raw materials that have been recycled, extracted (where possible) and refined in Europe. This could take the form of local content requirements, in combination with a "European Sovereignty Fund" aimed at securing Europe's strategic autonomy financed by the EU budget, as proposed by President Von der Leyen in her State of the Union annual speech. In addition, private investments should be encouraged and facilitated by State Aid support for projects that contribute to EU sovereignty in raw materials production, supply chain resilience and circularity. In the short term, the Single Market Emergency Instrument (SMEI) should also be considered to address immediate threats to the EU Single Market.

In this context, the upcoming EU Critical Raw Materials Act could play a key role in guaranteeing binding targets for European production of strategic materials, including aluminium. Europe has already lost over 30% of its primary aluminium production capacity over the past fifteen years, due to uncompetitive production conditions, often linked to high regulatory costs driven by ambitious environmental goals not mirrored in other competing parts of the world, and around half of the remaining capacity is currently offline due to the ongoing energy crisis. Unless Europe takes decisive actions to protect and improve the competitiveness of its strategic industries, there is a very high risk of permanently losing the European aluminium value chain.

Achieving strategic autonomy is crucial for the EU economy's future. To implement the European Green Deal, the EU needs to reduce dependencies by fostering domestic value chains and better diversifying low-carbon import sources. When engaging with international partners on trade negotiations and multilateral exchanges such as the G7 and the G20, securing strategic and critical supply chains should be a key priority. Relevant measures should therefore be taken to guarantee a continuous and viable supply of sustainably sourced and produced primary and secondary materials, such as aluminium.

Equal treatment between US and EU made goods and the need for effective carbon leakage measures

In its trade talks with the US, the EU must negotiate that EU/EEA goods[1] are ensured equal treatment with the US goods, as it currently is the case for Mexico and Canada, especially regarding the eligibility of raw materials under the scope of IRA. The EU and the members of the European Economic Area are longstanding trading partners and important allies of the US, and their supplies should not be discriminated. The IRA is set to unlock massive advantages for goods "made in USA" and this will put the EU competitors on an uneven playing field if no equivalent treatment is given to EU/EEA goods. If, in parallel, US industries are subsidised and European industries lose the current carbon leakage measures that protect them from unfair competition, the incentives to invest in the EU will be significantly reduced.

[1] EEA countries are integrated in and legally a part of the internal market. Countries like Norway and Iceland, as part of the European value chain, supply a significant amount of European's need for aluminium making products for export.

On this regards, the EU's Carbon Border Adjustment Mechanism (CBAM), presented as an alternative to current carbon leakage measures remains an untested tool, and it will not be effective for driving decarbonisation in the aluminium sector, or preserving industrial competitiveness. Removing the existing carbon leakage measures, i.e. the free allocation of allowances and the compensation for the indirect carbon costs, to replace them with CBAM, will increase the cost of producing aluminium in Europe by around 50%, and will not lead to a reduction of global emissions because European low carbon producers will continue to pay indirect carbon costs, while third country producers will face no cost at the border[2].

The EU needs measures that can truly protect the full European value chain against carbon leakage, and CBAM should therefore be introduced as a complement to existing carbon leakage measures. This would also ensure that European and US aluminium producers are on a level playing field with regard to carbon costs, while also facilitating the development of a "climate club" between the EU, the USA, and other like-minded countries.

Finally, if IRA is to become the investment tool used by the US in the context of the Global Arrangement on Sustainable Steel and Aluminium (GASSA) to address non-market behaviours and carbon intensity in aluminium and steel, there should be consistency with the EU's proposed CBAM and EU State Aid policy. In particular, when it comes to carbon intensity methodologies, the EU must abide to the principle that exemption to CBAM should only be considered if there is an explicit and equivalent carbon price paid in the country of origin.

The EU should be the leading voice in trade debates

The EU should take the lead on trade debates and keep on developing partnerships with like-minded partners adhering to the principles of fair trade. To protect the competitiveness of our industries, free trade agreements should promote the highest level of European environmental and social standards.

Raw material partnerships are a vital element to secure longstanding and cost-effective supply chains. Data show that European raw material sectors, above all the aluminium industry, are particularly exposed to unfair trade practices, such as dumping or state-subsidised overcapacities. Therefore, Europe needs to continue strengthening and, most importantly, enforcing its trade defence tools to level the playing field for European aluminium producers. For example, the EU should make better use of antidumping tools, by opening cases already at the "threat of injury" stage, well before industries are irreparably damaged or lost.

By speeding up actions, companies would be better and quicker protected, reducing the risk of production withdrawal. As we have seen in the case of magnesium, once European production stops, it is very difficult to re-establish it.

[2] See press release "CBAM Trialogues: Inclusion of indirect emissions could jeopardise Union's decarbonisation ambitions », November 2022 and 1 pager « Why including indirect emissions in the CBAM will lead to higher global levels of emissions », June 2022

Towards industrial funds & other supporting measures

European competitive soft funding and risk-reducing mechanisms are necessary to create a level playing field within the EU and beyond. European Aluminium encourages the use of instruments such as:

- Modernising EU state aid and opening up the possibilities for direct subsidies/tax breaks. To scale up the rollout of renewable energy in Europe, state aid should cover the whole value chain of renewables. The state aid procedure must speed up, specifically for those projects that are key for the green transition such as, for instance, the Green Pool[3].
- Taking inspiration form EU State Aid Policy and the State Aid Guidance on Climate Energy and Environment (CEEAG), one possible solution could be to harmonise at European level by means of Regulation and dedicated earmarking of new resources from the EU budget, tax incentives or reduction of energy surcharges to consume decarbonised energy, invest in circularity or invest in breakthrough decarbonisation technologies. Financing of such mechanism could come from the European budget or being co-financed with the support of an EU wide guarantee provided, for example, by the European Investment Bank.
- A European fund established by means of EU Regulation, to compensate ETS indirect carbon costs that energy intensive industries face in their power price. This should be accompanied by a clear set of rules establishing eligible undertakings, the exact amounts of funding available and time frame for receiving aid.
- Important Projects of Common European Interest (IPCEIs) to facilitate the roll-out of targeted raw materials projects in the EU, which would be labelled as of European interest, consequently benefitting from streamlined procedures and better access to finance.
- The idea of an European Sovereignty Fund is fully supported by the European aluminium industry and can be an important complement to IPCEI and other platforms.
- The InvestEU Fund to direct funding towards the whole European raw materials value chain. The policy windows of 'Sustainable infrastructure' and 'Small and medium-sized' could be geared up to direct funding towards strategic investments including Projects of Common Interest (PCIs). Such an action could direct more funding towards strengthening the EU's strategic resilience in raw materials.
- A dedicated lending platform for raw materials under the European Investment Bank. Lending, in the form of debt finance and loan guarantees, is a necessity to de-risk and crowd-in investments. The EIB could support increasing investment confidence and support the full raw materials value chains, by creating a dedicated thematic lending platform to boost the production and recycling of strategic and critical raw materials in Europe.
- The European Raw Materials Alliance (ERMA). As a principle, promoting and supporting ERMA's role in reducing Europe's raw materials' dependency on third countries and diversifying the supply from both primary and secondary sources, could direct a greater pool of public and private finance towards the European raw materials industry.

[3] The Green Pool proposal, a concept for decarbonising electro-intensive industries in Greece, would allow aluminium smelters and other electro-intensives to sign PPAs for renewable electricity, and is fully aligned with the EU's Green Deal agenda. Despite this, the state aid approval process has not yet progressed, and renewable PPAs have not yet been signed. State aid policy should particularly focus at immediately addressing the decarbonization challenges faced by the industries that are frontrunners in electrification, in order to incentivize further sectors to electrify their processes, where possible