Second strategic energy review

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Article 7 paragraph (c) of the Council Regulation (EC) No 405/2003 of 27 February 2003 concerning Community monitoring of imports of hard coal originating in third countries, requires the Commission to publish regularly a report on the market for solid fuels in the Community together with a market outlook. This Commission staff working document highlights the most relevant developments on the international and European coal markets during the years 2004, 2005 and 2006 and gives, as appropriate, trends and estimates for 2007.

The **main conclusions** from this report are as follows:

Coal in the World: from 2004 to 2006 total world coal production increased by 16% to 5 370 million tonnes (Mt). Updated analysis of proven coal reserves indicates that, at current world production levels, there is close to 150 years of coal available. A high proportion of world coal production is consumed within the country of origin – around 85%, and this is especially true of the two largest producers, China and the USA. Relatively small proportional changes in supply and demand in these countries can have a major impact on international market dynamics. From 2004 to 2006 world hard coal exports increased by 12 % to 815 Mt. For steam coal, the major exporting nations are Australia, Indonesia, Russia, South Africa, Colombia and China. For coking coal the major exporters are Australia, the United States and Canada. World steam coal exports rose by 11 % in from 2004 to 2006 to reach 593 Mt. Australia has retained its leading position in world exports with Indonesia second. In 2006, however, Russia overtook South Africa for third place. In 2007, world steam coal trade showed a further growth of around 4%. China became a net coal importer at the beginning of 2007 and South Africa showed some stagnation, but other producers increased their exports. World trade in coking coal decreased by 2.6% to 222 Mt in 2006. This followed growth of 8.6% in 2005 and 4.4% in 2004. Australia remained, by far, the largest exporter at 121 Mt. Further growth in crude steel production is expected for 2007 and demand for all coking coal qualities is expected to rise again.

Coal in Europe: Europe is the third largest region worldwide in terms of coal consumption, after China and the USA. Around two thirds of EU coal consumption is derived from indigenous production, with 164 million tonnes of hard coal and 454 million tonnes of lignite produced in 2006. Europe possesses substantial reserves of coal and lignite. World Energy Council figures show EU reserves of hard coal at 8.4 billion tonnes and lignite at 20.9 billion tonnes. Additionally, resource figures are assessed at 24.4 billion tonnes and 31.0 billion tonnes respectively by IEA. The largest hard coal reserve is in Poland, with significant reserves also in the Czech Republic, and lesser reserves in Spain, Hungary, the United Kingdom and Germany. In the case of lignite, reserves are present in a swathe from Germany through Central Europe and the Balkans, to Greece. Production of hard coal has continued its decline in the EU. Production reduced by 4.7% in 2005 (EU-25) and by 5.4% in 2006 (EU-27) and is expected to continue to decline in 2007. Hard coal consumption in the EU continues to be dominated by the power sector at 69% followed by coke production at 18%. In 2005, imports of hard coal to the EU-25 reached 192 Mt and represented 53% of total supply. The major exporting countries to the EU-25 were South Africa, Russia, Australia, Colombia, Indonesia the USA and Canada. In 2006, imports of hard coal to the EU-27 were 210 Mt, representing 56% of total supply. The most significant change in import sourcing from 2004 to 2006 is the major growth in imports from Russia.

Coal prices: steam coal prices strongly fluctuated in the period 2003-2007. They strongly increased in 2003/04 and again in the second half of 2007. Spot steam coal prices reached the level of $130 per metric tonne in December 2007 and their increasing trend continued in the first semester of 2008. Average import prices for steam coal in the EU rose less, from € 39 per tce in the first semester 2003 till €73 per

tce in the second semester 2007. It is expected that this average price will further increase in the 1st semester of 2008. Coking coal prices also remain high by historic standards. Chinese coke prices have increased dramatically in 2007 and towards the end of the year have approached $400/tonne fob, the highest level since May 2004.

Coal State Aid: due to unfavourable geological conditions, a part of EU indigenous hard coal production is not competitive with imported coal. After the expiry of the ECSC Treaty on 23 July 2002, the Council adopted a Regulation on State aid to the coal industry to provide a framework within which different kinds of state aid to the coal industry could be considered compatible with the EC Treaty from 24 July 2002 onwards. Over the period 2003/07 current production aid continued to decline.

Lignite: the world supply of lignite/brown coal went up by 0.9 % in 2006 and reached 913.8 Mt, following an increase of 1.3 % in 2005. Unlike the situation for hard coal, many European nations feature amongst the top producing countries. Europe is responsible for around 50% of world production, where it represents an energy resource of key importance. EU production of lignite has been fairly stable in the period from 2004 to 2006. With the inclusion of production from Romania and Bulgaria, the EU total lignite production was 454 Mt in 2006. Over 90% of lignite is used in power stations with the remainder being largely used for domestic heating, mainly in the form of briquettes. The increase in the import prices of hard coal is strengthening the competitive position of coal production especially in the lignite sector. This results in a more stable contribution to the security of energy supply.