

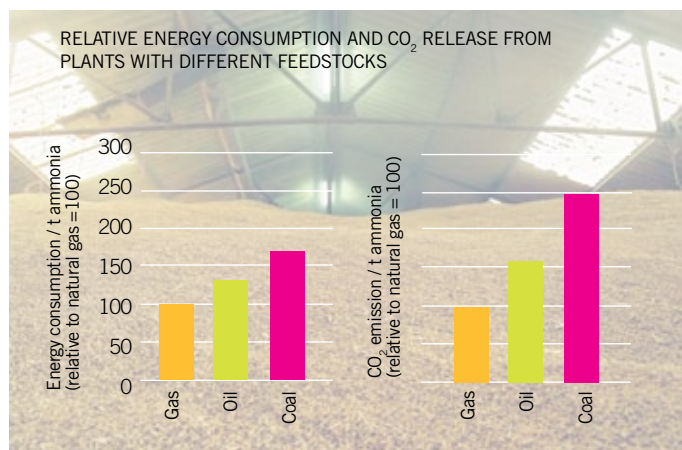
Dual pricing of natural gas penalises the European fertilizer industry with unacceptable costs

The security of the European fertilizer industry and Europe's food security is wholly dependent on a freely available and competitively priced supply of natural gas. Natural gas is an essential raw material for European production of mineral fertilizers which uses modern processes that conserve energy and reduce emissions. The practice of "dual pricing" of gas by Russia and some other producers remains a problem for the industry.

# Natural gas is an essential raw material for mineral fertilizers

The European fertilizer industry is the biggest single industrial user of natural gas in the European Union. Suppliers such as Russia, Egypt and a number of other countries currently operate a dual pricing policy on natural gas, whereby the price for domestic commercial and household users is heavily subsidised. In contrast, export prices for gas are set at a premium. This puts the European fertilizer industry at cost disadvantage to local producers in the global market, and has a major impact on the long term viability of the industry and Europe's food and fuel supply.

Natural gas is a fundamental raw material for modern fertilizer production and represents 50-70% of total feedstock costs. It is combined with nitrogen from the air to form ammonia, the principal building block of nitrogen fertilizers. Alternative production methods involving oil or coal are often less competitive and carry environmental disadvantages.



## FREE TRADE AND BETTER INFRASTRUCTURE

One of the guiding principles of the EU is the maintenance of free and fair trade. The reluctance of Russia to change its dual pricing policy on natural gas presents an obstacle to free trade and to its membership of the WTO. The country has again delayed its gas price reform programme to a new target date of 2015. At that time the government claims that prices inside Russia will be set on the

basis of equivalence to export prices to the EU, less transport costs netbacked to Russia. One of the current challenges is to restore a constructive dialogue based on compliance with "free market economy" principles.

In addition, there are a number of practical measures that can improve gas costs in Europe. There is an obvious need for new gas pipelines and LNG projects to supply the European market. A stronger infrastructure, based on strategic hubs with the appropriate pricing mechanisms, should provide greater access to gas producers/suppliers and lead to lower prices for consumers.

## LIBERALISATION OF ENERGY MARKETS

A number of EU gas reforms are under consideration to improve supplies and lower costs. The most important of these is the 3rd Gas Market Directive which covers ownership unbundling. This is proposed in three ways:

- 1) full ownership unbundling - a complete separation of generation/supply and transmission;
- 2) ISO (Independent System Operator), whereby assets can still be owned by the generation/supply company but control is transferred to an independent company;
- 3) ITO (Independent Transmission Operator), whereby the generation/supply company may still own and control the transmission operators but separate companies must be set up with separate interests and rules on asset management, staffing, identity and compliance control.

Current amendments to the original proposal include some important additional aspects. These cover support for low-carbon technologies, establishing European networks of transmission system operators, opening of gas storage to market players, transparent tariffs for use of transmission networks and gas storage, quality standards and better cross-border trade.

The establishment of new distribution companies, stronger independent national regulators, and a European agency to champion and control competitive conditions with reinforced powers, including sanctions, will encourage a more competitive gas market throughout Europe and benefit the European fertilizer industry and European agriculture.