

BRITISH ceramic CONFEDERATION

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Rt Hon Philip Hammond MP
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Dear Chancellor,

CERAMICS SUBMISSION FOR AUTUMN STATEMENT 2016

The British Ceramic Confederation (BCC) is the trade association for the UK ceramic manufacturing industry, representing the common and collective interests of all sectors of the Industry. Its 100 member companies (75% of which are SMEs) cover the full spectrum of ceramic products and comprise over 90% of the industry's manufacturing capacity. The sector in the UK employs about 20,000 people directly with at least as many in indirect jobs. Annual sales, including suppliers are around £2 billion with over £500 million exports. Members range from large multinationals to SMEs making products that will enable the recovery and improve the UK's balance of payments. Membership of the Confederation is extremely diverse - containing both foundation industries and advanced manufacturing / materials - including manufacturers of:

- Gift and Tableware
- Bricks
- Refractories
- Floor and Wall Tiles
- Clay Roof Tiles
- Industrial Ceramics
- Sanitaryware
- Clay Pipes
- Material Suppliers

We are encouraged by key points made by the Prime Minister¹: *"...I want to see an energy policy that emphasises the reliability of supply and lower costs for users. A better research and development policy that helps firms to make the right investment decisions. More Treasury-backed project bonds for new infrastructure projects. More house building. A proper industrial strategy to get the whole economy firing..."*. The recession exposed the need for a stronger manufacturing industry in the UK to rebalance the economy, increase GDP and generate export income. Each point is crucial in ensuring that the UK is seen as a competitive and attractive place for manufacturers to invest. Our submission offers practical policies / solutions to enhance the UK's 'investment credentials' by creating more business-friendly approaches to regulation, taxation, reporting and incentives (i.e. offering *"more carrot, less stick"*). This would, in the short term, help to bring economic stability by supporting opportunities for growth, including within our sector.

The consensus growth forecast suggest that in 2017-18 the deficit reduction is likely to stall, even without any discretionary policy action. Any discretionary fiscal measures might well lead to an increase in borrowing in the short term, but if effective, could provide real support to the economy, in the short and long term, making the fiscal position more-affordable in the long run. We understand the challenges and constraints faced by Government and the need for continued controls on Government expenditure. It is important however that this is not at the expense of investments in the country's future infrastructure, manufacturing or skill base. While we maintain that public finances should be balanced over the full economic cycle, we support a more-flexible fiscal approach this parliament i.e. not to reach fiscal surplus by 2019-2020. We therefore recommend temporary and targeted policy measures to support growth.

Your predecessor acknowledged that the planet will not be saved by shutting down the UK's energy intensive industries - we would only be exporting jobs. All energy-intensive industries face similar issues; and the **Ceramic EARTH campaign**² aims to ensure that this is recognised.

¹ Theresa May's speech in Birmingham (11 July 2016) "We can make Britain a country that works for everyone"
<http://press.conservatives.com/post/147947450370/we-can-make-britain-a-country-that-works-for>

² Ceramic EARTH Campaign – Update after Referendum
<http://www.ceramfed.co.uk/download/key-topic-1156.docx>

Our sector's full potential is not being realised because of a combination of policies. While ceramic exports have grown in recent years, the UK ceramic sector's overall trade balance stands at a deficit of almost £1 billion, and has grown steadily. UK Government can help reverse this trend, but we need a level playing field to compete internationally. We have five asks which require urgent and decisive ministerial action:

E	Emissions Trading Scheme. Whether part of the EU ETS, or as a separate scheme, the government needs to ensure all ceramic sub-sectors receive mitigation measures in full to guard against leakage of carbon, investment and jobs to competitors outside the UK.
A	Action to lighten the cumulative costs of UK energy, climate and environmental policies which harm the sector's ability to remain internationally competitive.
R	Reduce industrial CO₂ emissions by developing a long-term partnership with co-funding assistance for the sector to accelerate the development and implementation of breakthrough technologies.
T	Trade freely but fairly. Ensure an adequate and comprehensive UK-EU trade settlement obtaining, if possible tariff free access to the EU. New UK free trade agreements must support UK ceramic manufacturers. Develop adequate UK Trade Defence Instruments to protect UK manufacturers against dumped products. Reject unilateral EU and UK recognition of China as a Market Economy until it meets accepted criteria.
H	Housing. Achieve higher growth for the UK economy from government housing policy by enabling investment in the supply chain here rather than overseas.

EU ETS

The UK needs to take a holistic approach on issues affecting energy-intensive industries, working jointly across Government departments to prevent carbon, investment and job leakage. A combination of current policies is deterring investment and medium-term proposals could threaten business survival. Our businesses compete internationally and are at high leakage risks from unilateral UK and EU climate policy costs. The biggest deterrent for future investment to many of our businesses is the UK's policy support of 'tiering' of free allowances in the EU Emissions Trading Scheme (EU ETS) after 2020.

UK Government's proposals would mean that world class new energy-efficient brick, roof tiles and clay pipe factories would have to buy almost all their carbon after 2020; making them hugely uncompetitive compared with overseas competitors. The projected costs of carbon for this sector is likely to exceed profits in the 2020s for most ceramic manufacturing sites in EU ETS. Investment is being stifled at a time when there is strong product demand for construction materials for new homes.



Even with exciting local opportunities such as the 'Ceramic Valley Enterprise Zone' in Staffordshire with enlarged Enhanced Capital Allowances on offer³; excellent support from the Local Enterprise Partnership / local authority; market demand for products; low process emission raw materials; and good industry awareness, we are concerned that investment will prove very challenging because of potential ETS costs. Products where the UK has been largely self-sufficient for many decades are now seeing unprecedented levels of imports.

We are deeply opposed to tiering as it reserves mitigation for the handful of sectors in the top tier (e.g. steel) at the expense, sometimes grossly, of the vast majority of other sectors not in the top tier (e.g. ceramics). The introduction of tiering would also introduce major distortions with competitor products from other sectors in higher tiers; some of which are less durable and have higher embodied carbon emissions than comparable ceramic products. We need a fairer approach to ensure all Energy Intensive Industries receive adequate mitigation to guard against carbon, investment and job leakage risks. We need UK Government to wake up to the risks involved and pursue an approach which supports investment rather than kills off an industry that is capable of generating extra jobs and growth at this critical time in the UK recovery. At the very least UK Government must support full ETS carbon allowances for the most-efficient installations in all energy-intensive sectors. Even though HM Treasury does not lead on this policy, there is a responsibility to ensure

³ Ceramic Valley Enterprise Zone
<http://www.makeitstokestaffs.co.uk/locations/ceramic-valley-enterprise-zone/>

that the full economic consequences are understood on jobs, businesses, investments and costs if jobs are lost – and this has been lacking in work we have seen to date from any UK department.

The referendum outcome represents a major opportunity for the UK to shift to a holistic, novel and fairer approach to delivering industrial greenhouse gas emission reductions whilst enhancing the UK's competitiveness, jobs, growth and investment. We want to work with Government to explore a fairer approach.

Action to lighten the cumulative costs of UK/EU energy, climate and environmental policies

All UK ceramic businesses compete in fiercely competitive global markets and are at high risk of carbon, job and investment leakage. By their very nature, the international success of EIs is fundamentally reliant on competitive energy and carbon prices and therefore UK policies are required to achieve this. Divergence in these costs relative to competitors (both EU and non-EU) has already led to some relocation of production, loss of jobs / skills, financial costs to Government (e.g. benefit payments, lost revenue to HM Treasury) and the potential for net increases in global emissions. The current cost of energy and climate policy regime is extremely challenging for the UK ceramic sector and threatens company viability in the medium-term. Action on the following is urgently required if the sector is to retain an internationally competitive position:

- i) Adequate mitigation for the direct costs associated with greenhouse gas emission reductions.
- ii) A complete overhaul of indirect cost compensation associated with greenhouse gas emission reductions to ensure all electro-intensive sectors, subsectors and installations are protected.
- iii) Early repeal or phasing out of the 'UK-only' Carbon Price Floor (which is completely uncompensated for our sector). If this cannot be achieved, then at least the tax must be frozen permanently.
- iv) Extension of compensation / exemption arrangements from the indirect cost of renewables for very many more electro-intensive sites. UK industrial users continue to pay 80% more for their electricity than the EU average, yet only seven BCC member companies are compensated for some renewables costs, unlike many of their EU competitors (e.g. in Germany, Italy, Austria and France). We need a level playing field in both price and net tax. There is an opportunity to broaden this compensation at no cost to HMT as GB moves to an exemption in April 2017 by lowering the business test threshold.
- v) In the March 2016 budget there was no update on whether the Levy Control Framework (LCF) cap on low carbon energy spending will be extended beyond its current lifespan of 2020/21 although the budget did promise to announce further details in autumn on how it will control consumer bills. It is important that the longer term LCF cap is now clarified and that the cap is constrained to limit impacts on industrial consumers.
- vi) Compensation / exemption from the costs associated with the Capacity Market, transmission and balancing services attributable to renewable generation. These are a significant proportion of bills and are increasing. As yet these are unmitigated for our members, they would welcome support.

Energy security is essential to maintain business operations and long term investment certainty. At times of energy shortages, industrial users are particularly vulnerable, both in terms of the exposure to higher / more volatile energy costs and the major damage that can be caused to continuously operating high temperature kilns if gas or electricity supplies suddenly cease. Successive Governments have concluded that the market will deliver the UK's gas security. However, with no significant new gas storage capacity constructed in recent years coupled with Centrica Storage's recent announcement to extend the shutdown at its ageing Rough facility (which accounts for around 70% of total UK gas storage capacity), we feel Government urgently needs to reconsider the case for supporting new and existing gas storage facilities. One option for doing this is, as the Prime Minister said, using "*more Treasury-backed project bonds for new infrastructure projects*" as the market is not delivering the necessary investment. Our calculations allowing for a 30 year life, cost of capital, finance and gas indicate an additional cost to all consumers of 1p/therm. This is before factoring in the significant benefits of reduced energy price volatility and greater security of energy supply. Our members feel this is affordable for them. Government also needs to take urgent action to create a clearer pathway with timeframes / milestones for delivery of new electricity infrastructure.

Reduce industrial CO₂ emissions

Our work with Government on an Industrial Decarbonisation and Energy Efficiency Roadmap for the sector has shown the enormous challenge ahead to decarbonise and increase energy efficiency whilst remaining internationally-competitive. Major policy interventions will be required to meet emissions reduction required by the UK Climate Change Act and European legislative requirements. We believe that Government support is essential to develop collaboratively a supportive policy framework, encourage wider implementation of existing technologies as well to develop innovative breakthrough technologies. Decarbonisation must not mean deindustrialisation; and indeed, we would go a step further - decarbonisation should mean re-industrialisation.

We would welcome a range of measures to help boost investment, including in energy / carbon efficient manufacturing, including:

- i) Temporarily raising Annual Investment Allowances to £1 million until 2018 (CBI cost estimate £1 bn pa)
- ii) Energy efficiency grants – particularly for technologies with slightly longer paybacks than Boards and banks would normally cover. We have supported BEIS's application for up to £100 million (over the course of the Parliament) as a result of Roadmap work. Again this could be included as part of *"more Treasury-backed project bonds for new infrastructure projects"*
- iii) We have developed costed plans for an extension of the Energy Technology List (ETL) / Enhanced Capital Allowance (ECA) scheme to cover a wider range of technologies relevant to heat-intensive sectors (covering; "ovens", "heaters", "control", "insulation" and "heat recovery"). The annual cost to government (over a 5 year Government term, but excluding interest costs) is approximately £3 million for the ceramics sector. BEIS and the Carbon Trust are supportive of this approach and we have previously taken your officials through our analysis

We have been active in encouraging our members to apply for EU funding to deliver industrial decarbonisation, e.g. through Horizon 2020, SILC etc. However following a vote to leave the EU, access to these substantial EU funding streams will now reduce or cease. It is imperative that similar UK funding is forthcoming, e.g. via Innovate UK, Advanced Materials Leadership Council, Catapults etc. on a range of topics including energy reduction to develop commercially-viable "breakthrough industrial energy reduction technologies" applicable for a range of heat-using industries to meet our longer term emissions reductions targets. We stress that these must be grants and not loans.

The Regional Growth Fund (RGF) successfully benefited a number of projects within the ceramic sector. The objective of RGF was to provide financial support for private enterprises to lever additional funding to create sustainable private sector employment. Whilst welcoming the programme, we would have liked to have seen a broader scope of criteria to have been eligible, e.g. projects delivering energy / carbon savings and ring-fenced funds for this type of approach with broader benefits would be welcome in your autumn statement.

Trade freely but fairly

UK Ceramic manufacturers make products heavily traded across the world. Free trade is welcomed by our members, provided it is fair. The EU and UK are debating whether to confer 'Market Economy Status' on China which would prevent meaningful and adequate anti-dumping measures against unfair Chinese export practices and state intervention. We need the UK and EU to reject MES for China which only meets one out of five necessary technical criteria. Otherwise the change in dumping calculation methodologies could result in the direct loss of 300,000 jobs in EU industries - a third of which are in ceramics - already hit hard by dumped Chinese imports. The tile and tableware sectors currently have anti-dumping tariffs in place on Chinese manufactured goods. There are 6,000 UK direct manufacturing jobs in these sectors and many more in the UK supply chain including materials suppliers. We recognise that HM Treasury does not lead on this issue, but there is a responsibility to ensure impartial and fact-based analysis and objectivity is used in ascertaining whether China is or is not a market economy and not a largely political decision made without evaluating broader economic consequences on UK manufacturing and trade, both now and in the future.

With half ceramic exports sold in the EU, it is of no surprise that our members are anxious to avoid any tariff and non-tariff trade barriers that could make their products less competitive in this crucially important market. Other free trade agreements negotiated need to meet the needs of UK manufacturers.

Housing

It is very welcome that the Government has a clear objective to build more homes. The National Planning Policy Framework, revisions to Right to Buy and the introduction of Help to Buy and the Help to Buy ISA have all lent support for increasing homeownership. The Government's continued commitment to offer long-term certainty to increase the current housing stock is welcomed, however, construction product manufacturers must have confidence that these announcements will be delivered on the ground to ensure demand remains high, in the long term, to stimulate investment in manufacturing capacity. Further supply rather than demand side measures would be welcome.

There are significant economic benefits of retaining and growing UK production of construction products to meet a burgeoning housing need and maintaining alignment with the "UK Construction 2025 Industrial Strategy: Government and industry in partnership". More investment in new UK manufacturing capacity now needs to be made. This would also help boost productivity. A key target of this strategy is a 50% reduction in the trade gap by 2025 between total exports and total imports for construction products and materials⁴. If we

⁴ Balance of Trade - Construction 2025: Industrial Strategy: government and industry in partnership (July 2013)
https://www.gov.uk/Government/uploads/system/uploads/attachment_data/file/210099/bis-13-955-construction-2025-industrial-strategy.pdf (page 5)

get this right by working in partnership there is an opportunity to provide an additional 4,000 direct jobs, mainly in areas of high unemployment, and £300 million per year for the UK economy as well as capital investment of approximately £800 million. Our members would welcome working across Government departments to help ensure the essential principle of "Government and industry in partnership" is followed.

In summary, our submission proposes measures that would help: i) ensure economic stability, growth and investment; ii) UK Government to deliver on many of its commitments on decarbonisation and housebuilding; and iii) retain energy-intensive UK businesses through sustaining their international competitiveness. We do not want to see energy-efficient, highly-innovative UK ceramic manufacturers, driven from the UK given the opportunities for growth.

I hope that you find this submission of use and trust that explicit reference will be made to these concerns (provisionally, if need be) either in the Budget statement itself, or in additional material published at the same time. I would also welcome the opportunity to discuss these policy measures with you or your colleagues in further detail. We would be delighted if you would like to visit a ceramic manufacturing site so we can explain these issues at first hand.

Yours sincerely

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cc

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Rt Hon Sajid Javid MP, Secretary of State for Communities and Local Government
Rt Hon David Davis MP, Secretary of State for Exiting the European Union
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