

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(80) 707 Final

Brussels, 12 november 1980

Communication from the Commission
to the Council

The European Spot Markets for Oil Products

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Introduction

1. Government concern about the effects that exceptionally high prices on the Mediterranean and North-West European (the so-called Rotterdam market) spot market for oil products have on worldwide oil costs and on costs on domestic markets, led the Commission to study the structure and operation of these spot markets. The Commission has undertaken two separate examinations. The first was the re-introduction of the register of spot transactions that was operated for six months in 1978 under the name "Checkrun". This new register, called "COMMA" (Commission Market Analysis), ran from 4 June 1979 to 31 May 1980 at a total cost of approximately 500,000 EUA. It provided, through the voluntary participation of the industry, considerably wider coverage than the Checkrun and was organised to provide a deeper understanding of the market's structure and operation. The very detailed consultant's report on COMMA has already been forwarded for the information of the Member States.

This underlines the function of spot markets of balancing supply and demand at the margin and the fact that the NWE and Mediterranean spot markets are small in relation to the total trade in oil products in Europe. The main products traded were fuel oil and gasoil, each accounting for around 38% of the total. The total volume of spot transactions reported was 43 million tons, of which NWE reports accounted for three quarters and Mediterranean reports for a quarter. Taking into account that individual product parcels may be traded several times, the net spot trade in NWE can be estimated at 20 million tons (or around 5% of NWE consumption), about 50% lower than the results of the first Commission inquiry into the spot markets.

The second examination organised by the Commission was undertaken by a group of experts from different parts of the oil industry. Under the title of "The Bourse Group", these experts studied the possibility of establishing a formalised trading floor for oil products like a bourse or commodity exchange. Copies of the report prepared by The Bourse Group have already been forwarded to Member States.

The group noted that a market in the sense of an effective trading mechanism exists. It differs from an official bourse in that there is no registration of membership, no official registration

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or reporting of transactions (i.e. prices and volumes), no formal administrative body and no physical trading floor. But the existence of modern telecommunication systems renders the physical centralisation of trading unnecessary, an implicit code of conduct exists and price information is given by Platt's Oilgram and other publications.

The group did not consider that a bourse would significantly improve the way in which spot trade is handled and while the physical possibility of establishing a bourse is not contested, sufficient interest to allow the establishment of a worthwhile organisation cannot be expected.

In this context, the initiative of the London Commodity Exchange to establish a market in oil product futures, which is an interesting development, should be recalled and followed carefully.

2. Following the completion of the work of COMMA and The Bourse Group, the purpose of this communication is to outline the policy conclusions.

It should be recalled that spot market prices have an influence beyond the pure spot transactions because term deals, affiliate transfer prices and consumer price formulae are often directly linked to spot quotations. It should be the concern both of governments and private industry, while not impairing the essential economic function of the spot market, to improve market transparency and to avoid excessive price fluctuations, particularly in consumer prices and in those paid under long term contracts. In this context it would be useful to give thought to the possibility that prices of long term contracts should not only reflect spot market quotations as is often the case, but also take account of long term trends.

Price Reporting

3. The Commission does not consider that a price reporting system like COMMA should be maintained on a permanent basis.

Companies importing products already have to report for the register. Because of the modalities, in particular the volume cut-off, the register is not a substitute for spot market monitoring. However, reporting should be speeded up so as to provide effective information on average product import costs.

For the spot market as such, the Commission proposes that the ability to re-introduce COMMA for a short period should be maintained on a stand-by basis. This would be done in such a way that it could be quickly introduced at times of artificial disruption of the supply/demand balance.

In this way, public authorities will obtain quick and realistic information about spot market movements and in particular about the number of transactions involved.

Code of conduct

4. Buyers and sellers in the spot market have been concerned about governments' reactions to price volatility in times of tension and implied suggestions of irregularities and malpractices. Consequently, they were glad to participate in COMMA and demonstrate that they had nothing to hide. Now that COMMA is over they are keen to maintain government confidence in their trade practices. Because of this, it appears that market participants who wish to satisfy governments about their trading practices will be ready to adopt a suitable code of conduct, which would provide open and public assurance of their reliability and adherence to high ethical standards of trading practice. It is the Commission's view that any such development should be welcomed. Both by isolating those unwilling to accept the requirements of the code of conduct and by providing a relationship between those that do and government, a significant contribution towards maintaining better transparency would be made.

Summary and conclusions

5. a) There is no direct interest for governments in COMMA's being continued on a permanent basis.
- b) In periods of artificial disruption of the supply/demand balance, there is a need for greater transparency of the functioning of the spot market. It is proposed to establish the capability of re-introducing COMMA on a stand-by basis.
- c) It does not seem to be practicable to establish a formalised "Bourse" for oil trading, but the adoption by those that participate in the market of a specified code of conduct should be welcomed.
- d) Consideration should be given by market participants to the possibility that prices for long term contracts should take more account of longer term trends.

