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PAGE ONE
CONTINENTAL GUZZLERS
Europe's Big Cars Take Toll

**New Regulations Loom
 As CO2 Emissions Cut
 Falls Behind Schedule**

By **STEPHEN POWER**
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BRUSSELS -- European Commission President José Manuel Barroso says it's time to "attack the problem of climate change."

But for his own family, political Europe's chief executive owns a vehicle that's hardly saving the planet. The family ride is a Volkswagen Touareg -- an SUV that, in its most-efficient version, emits 1.6 times the average level of carbon dioxide for new cars from Europe's manufacturers. To demonstrate how powerful the Touareg is, Volkswagen recently used one to tow a 747.

Despite paying sharply higher fuel taxes than Americans, Europeans are driving faster, heavier, more-powerful automobiles than they did in the past. SUV sales are rising in Europe, and amid growing price competition from Asian auto makers, buyers are demanding vehicles with weight-adding features such as air conditioning.

That trend is jeopardizing Europe's green credentials and undermining its pledge under the 1997 Kyoto Protocol to reduce emissions of greenhouse gases to 8% below 1990 levels by 2012. Although the EU has cut overall greenhouse-gas emissions by nearly 5% since 1990, CO2 emissions from cars and commercial trucks in Europe have risen more than 20% -- offsetting much of the savings in other sectors. According to the U.S. government, emissions of greenhouse gases have increased by 16% in the U.S. since 1990.




Jose Manuel

The auto industry's inability to cut CO2 emissions in Europe fast enough is putting it on a collision course with regulators. Next week, the European Commission is expected to consider a proposal to impose new CO2 regulations that some experts say could raise the retail price of a new car in Europe by €3,300 (about \$4,300) on average -- a blow to Europe's beleaguered car makers, and a departure from the EU's traditional reliance on voluntary efforts by auto makers. Any regulations would likely also apply to U.S. and Asian car makers.

The dispute in Brussels over how to reduce auto emissions is taking shape amid a global debate over how to cut emissions of greenhouse gases. It coincides with a spate of warnings that have renewed public attention to

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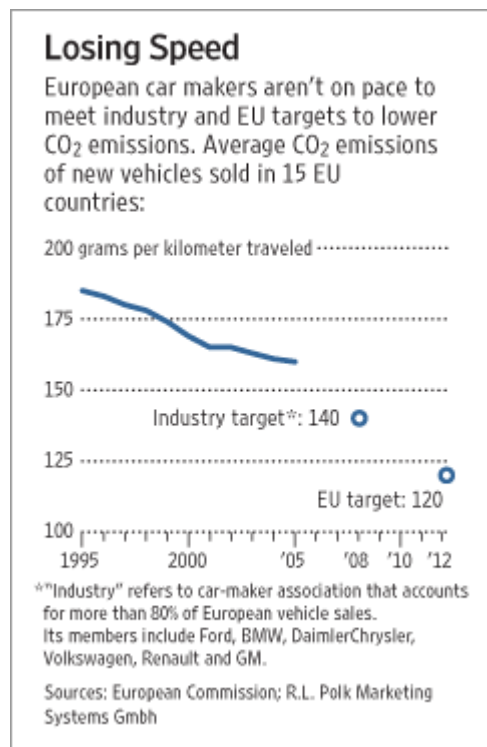
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climate change, including the collapse of an ice shelf near the North Pole and the Bush administration's recent proposal to classify the polar bear as a threatened species amid concerns about melting ice.

In the U.S. -- where the Bush administration doesn't treat CO₂ as a pollutant as Europe does -- the newly Democrat-controlled Congress is putting climate change high on its agenda. The Supreme Court is weighing whether the Environmental Protection Agency has the authority to regulate car makers' CO₂ emissions. California and some other states, meanwhile, are moving forward with their own plans to reduce CO₂ emissions from cars.

In Brussels, the next step could well be mandatory cuts intended to reduce average CO₂ emissions from new cars by more than 20% from current levels, to 120 grams per kilometer over three to six years. For auto makers, that proposition -- bound to entail investments in fuel-saving technologies and reductions in sales of their biggest, most-profitable vehicles -- comes at a time when Europe's auto market is racked by intense price competition, weak demand, and underutilized factories.

"You can't sustain this industry and millions of jobs if you say by 2010, 120 grams is the regulated result," says **DaimlerChrysler** AG chief executive Dieter Zetsche.



Any effort to impose CO₂ regulations is likely to generate fierce resistance, particularly in Germany. One out of seven jobs in Europe's largest economy depends on the auto industry. German manufacturers -- including DaimlerChrysler's Mercedes unit, **BMW** AG, **Porsche** AG, and **Volkswagen** AG's Audi brand -- are particularly vulnerable because their lines are thick with vehicles that have heavy engines and churn out relatively high CO₂ levels.

To reduce CO₂ emissions as quickly as some EU officials would like, sales of some of the heaviest, most-profitable vehicles would have to fall by 10% -- a step that would cost BMW roughly \$650 million a year, according to a recent analysis by Citigroup Inc. That's more than BMW's net profit in the third quarter of 2006. Research by experts hired by the European Commission indicates the price of a new car in Europe would rise, on average, about \$4,300 if the industry is required to reduce average CO₂ emissions from new cars to 120 grams per kilometer by 2012. Environmentalists say those costs would be more

than offset through savings at the pump from improved fuel economy.

Since 1998, the European Commission has relied on an industry pledge to cut average CO₂ emissions from new cars by 25% from 1995 levels by next year. At the time, European Commission officials said a voluntary approach would give companies flexibility to achieve the target in the most cost-effective way.

But several trends have slowed auto makers' progress. With customers demanding more features and performance, the average weight of new cars in Europe has risen nearly 15% since 1999, while average horsepower has grown by nearly a third.

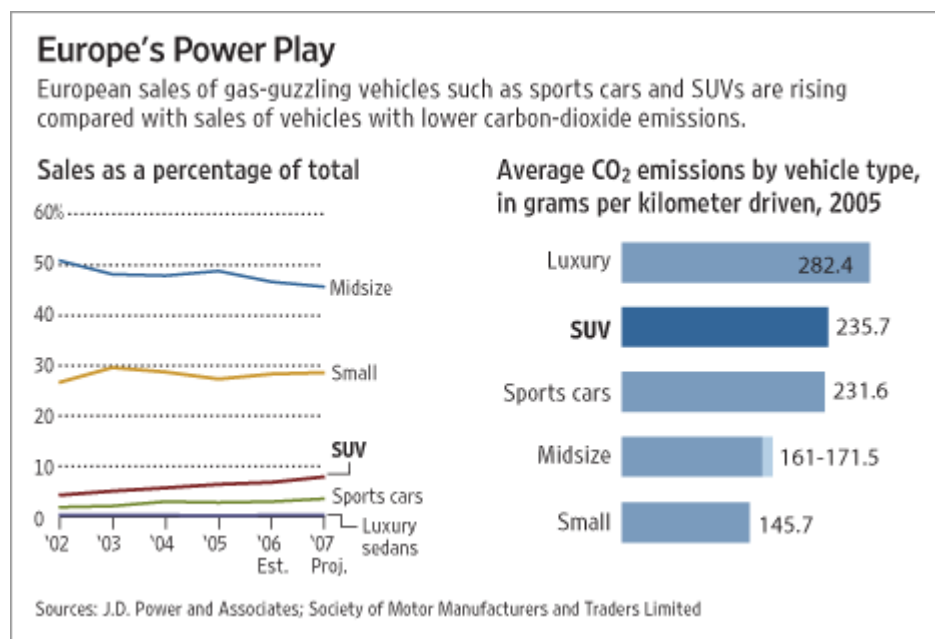
Sales of SUVs -- which typically consume more fuel, and thus emit more CO₂ than small cars -- are up. They account for roughly 6% of new sales in Europe and are projected to grow to more than 10% by the end of the decade, versus less than 3% in 1998. (In the U.S., SUVs account for roughly a quarter of automobile sales.)

The bottom line: The industry risks falling short of its pledge. A recent study commissioned by the European Federation for Transport and Environment found three-quarters of all car brands in Europe have failed to improve their fleets' fuel economy at the rate needed to meet next year's target.

"We're not on track...it's absolutely necessary we have binding regulations," says Pieter van Geel, the Netherlands' state secretary for housing, spatial planning and the environment.

In theory, cutting a car's CO₂ emissions is as easy as improving a vehicle's consumption of fossil fuel.

But in an echo of long-running debates in Washington over promoting fuel economy, auto makers in Europe are warning of trade-offs between safety and the environment. Industry officials complain new EU safety rules have made it harder to reduce CO₂, by adding weight to cars and making them less aerodynamic.



Among the most ballyhooed changes is a 2005 EU rule that seeks to reduce pedestrian deaths and injuries by setting minimum heights between car hoods and engines. The rule is intended to soften the impact when a pedestrian's head hits the hood of the car. It forces manufacturers to leave more "crumple room" in designs.

Industry officials say the rule undermines fuel economy by encouraging them to install features that add weight, such as collision sensors. Some environmentalists and safety experts say the industry is exaggerating the weight impact of safety rules and that weight increases have been driven more by comfort features.

Europe's gasoline taxes haven't been enough to deter customers from heavier, more-powerful vehicles. Although a gallon of gas in Europe costs more than \$5, compared with \$2.31 in the U.S. as of last month, the cost of owning and maintaining a car in Europe has been falling for years, thanks to better-designed engines and the growing percentage of cars that run on diesel, which tend to be more efficient than those that run on gasoline.

Another reason Europe's auto makers are having trouble cutting emissions: competition. Asian rivals like **Toyota Motor Corp.** now account for more than 17% of new-car sales in the region, compared with 14% in 1999. The competition is leading to deals on features that add weight, such as air conditioning and navigation systems. Nearly 90% of new cars sold in Western Europe now come with air conditioning, compared with 70% in 2000.

Many car makers also are rushing to add SUVs to their lines, including companies better known for small cars or sporty sedans, such as Volkswagen and **Renault SA**.

"It is so nice and big, and I sit up high," Ingrid Fischer, a 52-year-old mother of two in Kamp-Lintfort, Germany, says of her Mercedes M-Class SUV. She says she doesn't dwell on the M-Class's CO2 output -- 249 grams per kilometer, compared with the average of 161 for new cars made by European manufacturers.

The dilemma facing European policy makers stems from a 1998 deal with the European Automobile Manufacturers Association, which includes **General Motors Corp.** and **Ford Motor Co.** The group agreed to reduce average CO2 emissions from new cars by 25% by 2008, compared with average emissions of new cars sold in 1995. A year later, EU regulators negotiated a similar accord with Japanese and Korean auto makers.

To cut their CO2 emissions, car makers accelerated production of small cars. Promoting its Lupo, introduced in 1999, Volkswagen staged a cross-continental journey billed as the most fuel-efficient road trip in history.

But in a few years, sales of Europe's smallest cars weakened, falling 8% to 1.34 million units in 2001 from 1.47 million in 1999. Although demand for Europe's smallest cars has begun to pick up recently, sales remain well below the highs achieved in the late 1990s.

"The trends went against us," says Wilfried Bockelmann, former director of technical development at Volkswagen. The Lupo derived much of its fuel savings from lightweight but costly materials such as aluminum that drove its price to more than €15,000. "It was a great car, but too expensive," says Olaf Brey, a Volkswagen dealer in Berlin. Volkswagen stopped producing it in 2005.

As sales of the smallest models cooled, demand for SUVs roared. In London, the mayor derided SUV drivers as "idiots." Traffic congestion there has grown so prevalent that the city in 2002 set a daily fee of £5 pounds (\$9.87) for drivers entering the city's heart.

But for many Europeans -- particularly older customers -- the shift to bigger, more-spacious vehicles seemed only natural.

"The seats of all the cars I had so far are much too low for me, and this made it difficult for me to get in and out with my aching back," says Rainer Haase, a 65-year-old retiree in Berlin who replaced his 13-year-old BMW 7-Series sedan with a Toyota RAV4 SUV.

The industry's rate of CO2 reductions is threatening to complicate the pro-business agenda of Mr. Barroso, the European Commission president and a former Portuguese prime minister. Since taking office in 2004, Mr. Barroso has pledged to reduce the regulatory burden on business -- often seen as one of Europe's economic drawbacks.

But some say the continent's experience with car makers shows the need for more government involvement, not less. "Considering the failure of the voluntary agreement, it seems the European Commission will have to legislate," says Patrick Coroller of France's Agence de l'Environnement et de la Maîtrise de l'Énergie.

Mr. Barroso, through a spokesman, declined to be interviewed for this article. In written response to questions, he said "not enough progress has been made by European car manufacturers" and "we will therefore set a series of options on how to ensure that the targets are met."

As for his own choice of vehicle, Mr. Barroso added, "Product choices are up to individuals, according to their personal needs and preferences. It is against the European concept of a free society to micromanage people's choices according to one model of supposedly correct behavior decreed by self-appointed moral authorities."

One idea gaining ground among regulators is an emissions-trading system in which companies would get credits for producing cars with low CO2 levels. They could then sell the credits to other companies. Such a system would benefit makers that specialize in small cars and possibly force others to reduce the weight of their vehicles or pay extra for the right to churn out vehicles with high CO2 levels.

The auto industry, meanwhile, is prodding EU officials to promote clean-burning fuels that emit less CO2 than gasoline, possibly through a Europe-wide tax scheme based on a fuel's carbon content.

"It doesn't make sense to look at just the car," says DaimlerChrysler's Mr. Zetsche.

Forging consensus on taxes across the EU won't be easy. Some members are already crafting their own tax schemes to cut CO2 -- a development that frightens the industry.

--Almut Schoenfeld in Berlin and John Fialka in Washington contributed to this article.

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