

CHALLENGES FOR THE EU BIO-ETHANOL FUEL INDUSTRY



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F.O.Licht's World Ethanol 2005

Amsterdam, 2-4 November 2005

Ladies and gentlemen,

eBIO is very honoured that it is invited to address the most important ethanol conference there is and to share with you what we think are the challenges for our sector.

In my presentation I will bring you up-to-speed on what is happening in the European bioethanol fuel sector: where are we coming from, where we are now and what can be expected to be the way forward. The latter involves some speculation given several elements of uncertainty or challenges. I would like to address these in the second part of my presentation. Finally, I would like to indicate what needs to be done in Europe to make sure that we will see in Europe a bright bioethanol fuel sector and market comparable to what we witness in Brazil and the USA today.

But before I start with informing you on the state of play first a few words on **eBIO**.

eBIO is short for the European Bioethanol Fuel Association. It is a company composed interest group that focuses on the promotion of bioethanol for fuel use only. All other applications of ethanol from bio-origin do not concern **eBIO**. To this end we maintain frequent contacts with the European legislative and regulatory key institutions such as Council (Member States), European Parliament and European Commission: from the desk policy officer to the relevant European Commissioners, members of Parliament or government ministers, but also numerous non-governmental organisations (NGOs).



- Founded in 2005 by 6 companies
- Non-profit international association fostering bioethanol fuel production and use in the EU and advocating the proper legal and regulatory framework
- New members from Belgium, Austria, Hungary and UK per 1-1-06

Founded earlier this year in Seville **eBIO** brings together 6 companies: Spanish Abengoa Bioenergy, German Südzucker Bioethanol and KWST, Swedish Agroetanol, Dutch Royal Nedalco and UK Wessex Grain or Green Spirits Fuel. From 1st of January 2006 there will be new members from Austria, Hungary, Belgium and the UK.

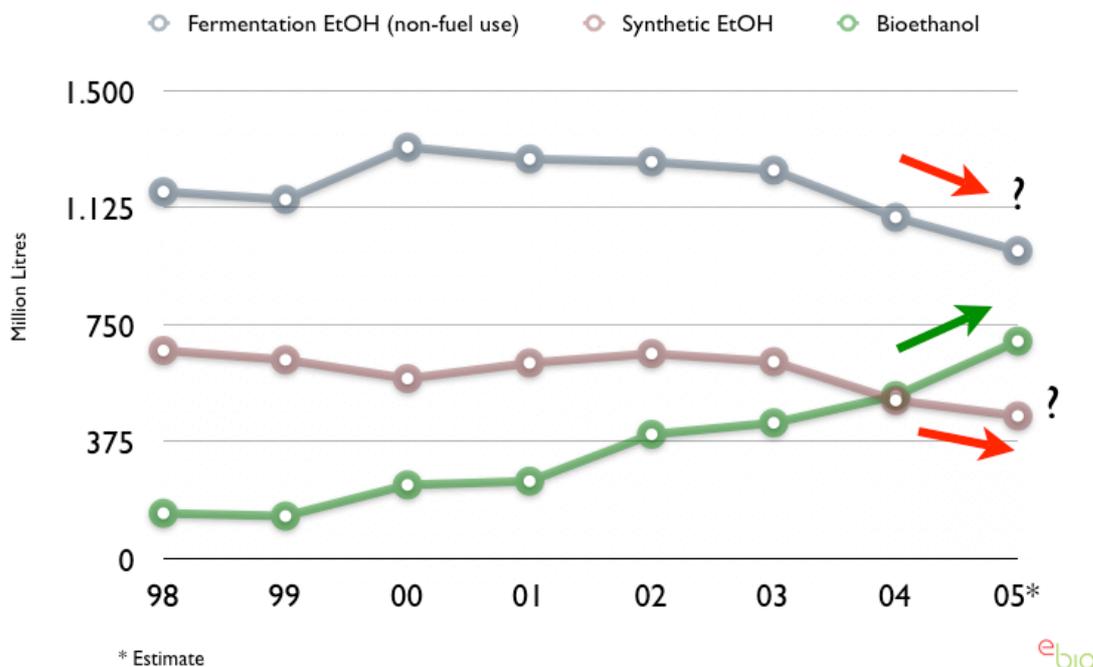
The membership of **eBIO** is open to all EU based companies that are engaged in the production of bioethanol fuel or are planning to install production capacity in the near future. Next to these producing members there are also associate members (such as KATZEN International) representing companies or organizations that do not produce bioethanol fuel but have a certain interest in promoting it.

Now let's have a look at the state of play of EU bioethanol fuel production.

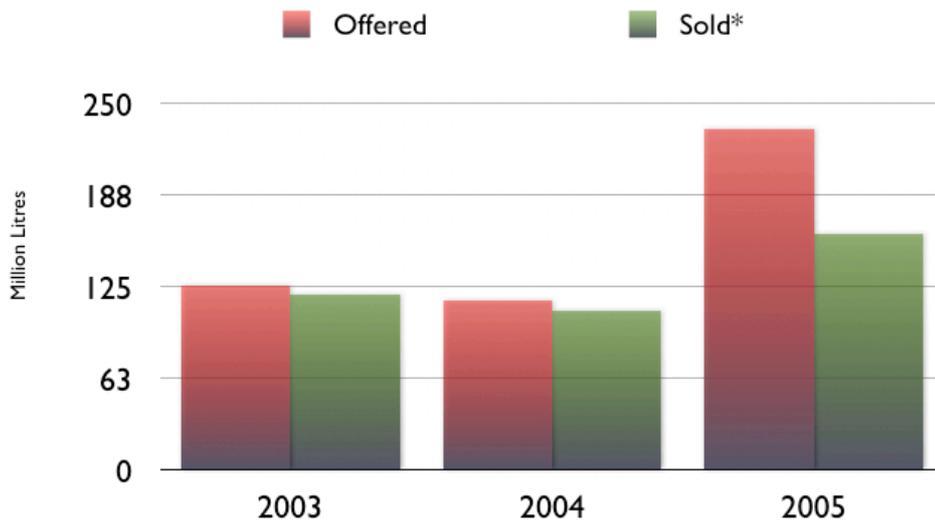
State of play

Since 1993 we have seen in the EU an important growth in the production and use of bioethanol fuel, relatively speaking. Where the other ethanol markets (beverage, industrial) see no growth and are even shrinking, **EU bioethanol fuel production** went up by 9 times from 60 m l in 1993 to 526 mln l in 2004. Very likely this year we will see an important step forward to a 'guesstimated' 700 mln l representing a 33% increase. This increase can be explained by higher production in France due to new government support, thanks to crisis distillation measures in the wine sector resulting in a much bigger volume of wine alcohol on the market, and a growth in Germany because of new production capacity.

EU Ethanol production



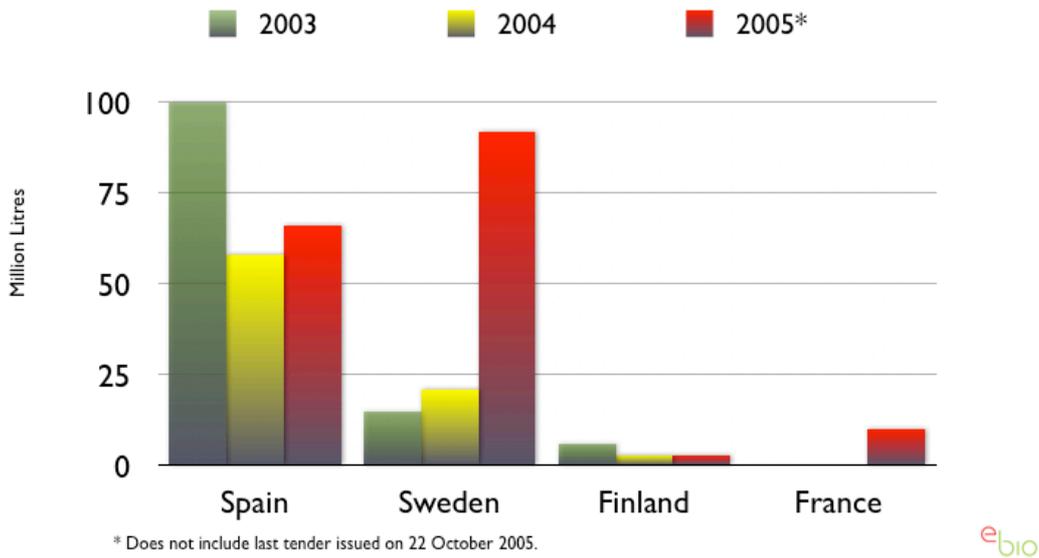
Wine Alcohol for fuel



* Does not include last tender issued on 22 October 2005.

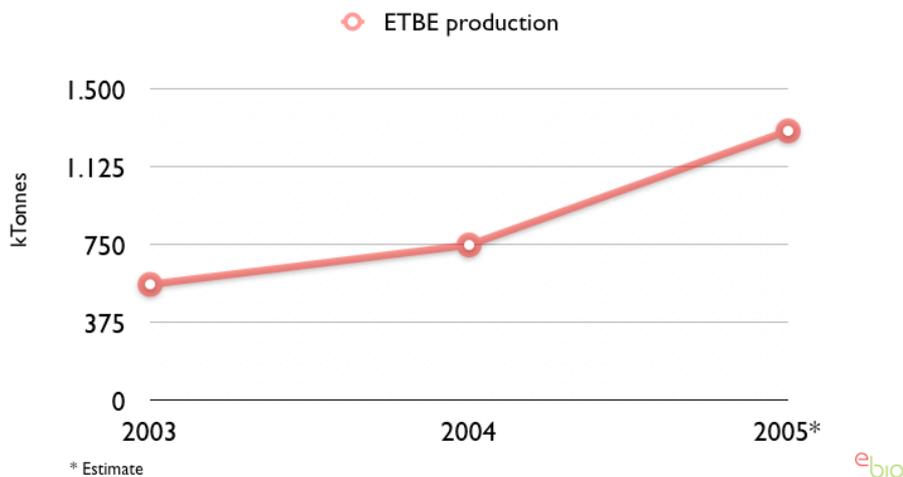
The **wine alcohol** needs some further elaboration. In 2004 the Commission offered for sale in the EU fuel market a total volume of 116 mln l. Of this 85 mln l went to Spain, 21 to Sweden, 3 to Finland and 7 mln l was not sold. This year, to date, already over 230 ml has been offered and 171 mln l sold through a tender procedure. Countries of destination: Spain (66 mln l), Sweden (92), France (10) and Finland (3 mln l). What we see is that wine alcohol offered for the fuel market increased by 98% and that its use increased by 56%. In Sweden use more than quadrupled. Also the price increased. In 2003 the average price per hl was 20.5 Euro, this year it was 32.2 Euro an increase of 57%. In the near future destinations may well change, due to a growing number of companies that will participate in the tenders. But also the yearly volume will change: a reform of the wine regime planned for next year should lead to substantially less crisis distillation measures.

Wine Alcohol for fuel



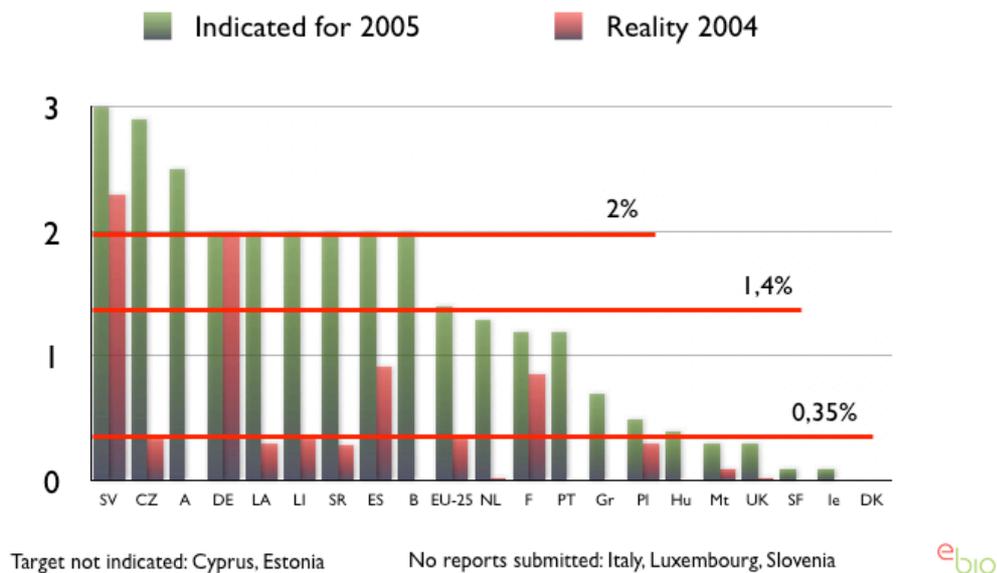
At the **ETBE-side** we also see growth. In 2003, production was 560 ktonnes going to 750 ktonnes in 2004 and an expected output of 1.3 million tonnes this year. Highest growth numbers we will see this year in Germany to 400 kt up from 120 kt and Belgium 180 kt up from zero.

ETBE Production



Even with this strong production increase for both bioethanol fuel and ETBE the overall biofuel consumption in the EU is still far from achieving the 2005 2% target set in the Biofuels Directive. This slide shows a comparison between what the Member States indicated to the European Commission to be their national target in 2005 (the first bar) and what was achieved last year (second bar). We see that just 2 countries have been able to achieve the 2% last year: Germany, thanks to biodiesel and Sweden, thanks to bioethanol. A majority of Member States show a rather poor result bringing the average for 2004 to a shameful 0.35%. For sure, this year the result will be much better, the Commission believing that an average of 1.4% would be reached. Personally, I think that this is still rather optimistic.

Biofuels Target



The good news is that Member States have caught the biofuels fever. Whether the driver is increasing oil prices or the fear for the name and shame policy of the European Commission, who is threatening to go to Court if Member States do not comply, does not matter. What matters is that:

- 1) The group Member States that puts in place a biofuels policy and tax credit is now outnumbering the group of countries that is lagging behind.
- 2) Both investments and the number of investment plans for bioethanol fuel plants are growing. At present installed EU bioethanol fuel production capacity is about 1 billion litres. If we look at plants being built and announced investments this number will go up to 1.5 billion litres next year. A major leap forward is to be expected in 2007 when production capacity could well go over the 4 billion litres threshold. The year after 4.5 billion litres could be expected.

However, before we get there and grow further some sticky problems need to be solved. Or to put it more positively: we are facing as an industry some tough challenges.

Challenges

The challenges the bioethanol fuel is facing are of very different nature.

Trade

The big issues in this respect are recognizing the sensitivity of the product and secondly to bring about a EU import policy that is balanced.

The EU in general believes in trade flows with as little as possible barriers, be it tariff or non-tariff. For developing countries, more in particular the poorest (LDCs), there shouldn't be any obstacles at all. The Cotonou Treaty for ACP countries and the System of Generalized Preferences (GSP) are the preferred instruments to achieve these goals for privileged countries and the WTO for all the rest. As a result of Cotonou and GSP at least an equivalent of 10% of domestically produced ethanol enters duty free the Community. For now, only a very small volume of this enters the fuel stream. If, however, the same free trade philosophy would apply for those countries that are the main producers of ethanol in the world the EU bioethanol industry would not ever reach the stage beyond an infant industry. Therefore, an infant industry, should, like is normal for infants, develop in a favourable environment.

Both Commission and Member States should in their trade policy (WTO, GSP, bilaterals) take account of the very nature of the EU bioethanol fuel industry as well its inability yet to compete at global level. Recognizing the sensitive nature of the product would be a sensible policy. As soon as the industry is mature and able to compete trade barriers could be dissolved step-by-step.

Fuel quality specifications

Getting the fuel quality specifications right is crucial to come to economies of scale and a mature bioethanol fuel sector. The Fuel Quality Directive in force (98/70) sets explicit limits to the development of bioethanol fuel. Due to this there is a clear inconsistency in EU law between what is stipulated in this Directive and the Biofuels Directive (2003/30) which makes it very doubtful that the 5.75% target will be achieved.

We are confronted with 4 limitations:

- The overall oxygen limit is set at 2.7% mass, which means that the total ethanol volume (direct and through ETBE) is also limited.
- The maximum direct blending percentage that can be used is set at 5% vol..
- As regards ETBE the maximum is 15% vol..
- Finally, there is a vapour pressure limit that makes direct blending difficult without a waiver as has been adopted in the USA. Oil companies could of course adjust their base petrol to avoid this RVP problem, but there are costs involved.

If we want the bioethanol fuel market to grow than these limits will need to be abolished or relaxed to the measure possible. If we want to achieve ambitious targets both ETBE and direct blending are necessary in higher volumes than allowed now.

Therefore, the European Commission, Member States and Parliament should understand that directly blending ethanol in petrol, beyond countries like Sweden and the UK or other arctic regions, requires a different set of specifications. We expect the Commission to come with their review beginning of next year and we are confident that it will propose to adjust present specifications in such way that bioethanol use in petrol will become easier.

Incentives

Looking at the recently adopted US Energy Bill one will find a raft of incentives to help the industry to grow further. In this respect EU member states fail enormously. We have to be far more creative. It needs to be more than detaxation the biofuel to compensate for the extra costs.

Providing grants and credits for getting the right infrastructure in place, subsidies for bioethanol driven flexy fuel cars (like the hybrid car), no road and/or congestion tax, building captive government owned fleets, subsidies for flexy pumps, grants to develop R&D and build pilot plants are all very necessary to eventually achieve economies of scale that will make the bioethanol fuel industry more competitive and the bioethanol fuel more attractive to use.

Support

We will not get very far unless both industry and public authorities will be able to convince the public at large that the (support and) use of biofuels is the right thing to do. Our message to the consumer is that the use of renewable motor fuels such as bioethanol fuel can deliver the best contribution to bringing down green house gas emissions immediately and achieving the Kyoto goals.

Especially important in this respect is to win the unequivocal support of NGOs that advocate green policies. By addressing key members of both national and European parliaments and building within these parliaments support groups for biofuels this public support can be partly and indirectly realized.

Global challenge

It is obvious that Brazil made a good headstart already 30 years ago. The 25% blending obligation combined with the stunning success of the Total Flex car and growing export opportunities make Brazil enter the era of the bioethanol Bonanza. The USA earlier this year got its act together. These developments confront EU producers with a growing competitiveness problem that needs to be addressed rapidly by EU Member States.

Both Commission and Member States need to understand that there is too much regulatory and fiscal fragmentation in Europe hampering the development of a strong EU-based production. The fragmentation should stop. We need Europe-wide obligatory targets. On top of that we should see a decision to have a minimum of 10% biofuel in petrol.

These have been **eBIO**'s core messages to several European Commissioners we have seen in recent weeks. These are also the messages the European Commission needs to reflect in its new biofuels policy document it is going to publish at the beginning of next year.

Way forward

The members of **eBIO** have established a strategy and action plan for the coming 5 years as well as a work programme for this year and next year to address these challenges. The strategic plan identifies 6 areas on which we will focus our work.

Allow me to say a few words on these 6 areas at the same time summarising my presentation.

1. Reducing market uncertainty and improving price competitiveness.

In this respect is crucial (a) realising a EU import policy on bioethanol fuel that is in line with what the EU bioethanol fuel market can bear (b) creating a public friendly investment climate that assures investors a decent return on their investments (c) increasing R&D funds for lignocellulose to bioethanol fuel.

2. Removing regulatory barriers.

This means: (a) remove or increase allowed oxygen content in petrol, including level of bioethanol and ethers, (b) adjust volatility specifications to allow for low level direct blending.

3. Promoting ethanol blends in other kinds of transport systems.

By (a) Using bioethanol in diesel engines for 2 reasons: (1) as the EU is short on diesel bioethanol could reduce import dependency and (2) contribute to reducing CO₂-emissions of diesel as well as particulates. (b) Developing a EU standard on bioethanol in diesel.

4. Raising public awareness.

We will advocate for public fleets running on biofuels, a change in government procurement, visibility of using renewable motor fuels by using labels at filling stations, and incentives for users of E85 cars (less road tax, no congestion tax or road tolls, subsidy for buying such cars, etc.).

5. Addressing inflexibility in the transport system.

In this area we will focus on measures that will make bioethanol fuel an integral part of the transport and fuel system, like introducing flexi-pumps.

6. Calling for Bioethanol to hydrogen R&D.

Finally, calling for R&D funds to optimise the bioethanol hydrogen processor and its application in service stations and vehicles.

Wrapping up

Let me come to the wrapping up of my presentation.

What we see is that the EU bioethanol fuel market is progressing and that the number of Member States putting up supportive measures is growing too. This well fits within the global dynamics of the biofuel sector. However, compared to what is happening in other parts of the world, especially Brazil and the USA the EU progress is not enough. The only way forward in the European Union to obtain the much needed level-playing field is that Member States introduce the same sort of obligation we see in those 2 countries. If the industry is not able to convince the European Commission and Member States of this policy need, we in Europe will not reduce our dependency on fossil oil for transport nor achieve the goal of climate change or contribute to new opportunities for sustainable rural development.

The European Parliament has understood this message very clearly as it recently adopted a resolution in which it called for ambitious mandatory targets to increase the share of alternative energy sources. **eBIO** can only but support the European Parliament.

Later this month the European Commission will release its Biomass Action Plan. In this Action Plan the Commission will propose a series of measures we have been advocating during this year. eBIO is also confident that the new Biofuels policy document to be released in January 2006 will have the same clear messages and measures that we need to get a strong, competitive European Bioethanol Fuel sector.

The time is right. Europe should get his act together. We should do what Brazil is already doing for 30 years and what has recently been adopted in the USA: the obligatory use of renewable motor fuels. It is possible. The only thing we need is the political willingness to do it.

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