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« Biofuels in Europe and the United States: Energy, Economics, and Trade Aspects ? »

ICONE
Institute for International Trade Negotiations

U.S and EU Policies on Biofuels: Potential impacts on Developing Countries

A study commissioned by the German Marshall Fund of the United States

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Background

- Absence of specific customs classification for biofuels

- Trade in biofuels is currently very limited…..
  - US imports of ethanol (05/06) = 2’850 mn liters (MTBE ban effect)
  - EU imports of ethanol (2006) = 230 mn liters
  - Brazilian exports of ethanol (2006) = 3’028 mn liters

……But it could increase significantly in the coming years,

BECAUSE

- Demand is expected to scale up in developed countries to limit the use of fossil fuels. But production capacities are limited by a range of constraints.
- Tropical and sub-tropical developing countries have a real comparative advantage in the production of feedstock that is more suitable for biofuels production.
- Since supply and demand are not located in the same places, there should be room for significant increases in international trade flows.

Outline

- Main barriers restricting current and potential biofuel exports from developing countries
- Drivers that could increase biofuels imports in developed countries in the medium run (2012)
- Limitations on the export potential of developing countries

Main Barriers Restricting Current and Potential Biofuel Exports from Developing Countries

Tariffs

MFN tariffs	U.S	EU
Ethanol	2.5% + 0.14 US$/liter (46% EAV)	0.192 €/liter (63% EAV) 0.102 €/liter (39% EAV)
Biodiesel	4.5%	6.5%

Preferential tariffs

- EU – ethanol:
  - Free access for: ACPs, GSP+, LDCs, Western Balkan countries.
  - No access for current/potential big players: Brazil, Thailand, etc.
- EU – biodiesel:
  - Free access for ACPs, GSP, GSP+,LDCs, South Africa, Chile, Western Balkan countries, etc.
  - Tariffs on vegetable oils are very low: between 0 and 6.1%
- US - ethanol:
  - Free access for: Mexico, CAFTA, Colombia, LDCs, etc.
  - Caribbean Basin Initiative (CBI):
    - More than 50% local content: duty free, quota free
    - Less than 50% local content: 7% of US consumption
  - No access for current/potential big players: Brazil, Thailand, etc.

Subsidies

- Support to feedstock
  - US
    - Subsidies to corn in 2004: 36% loan deficiency payments, 22% countercyclical payments, 20% fixed payments under historical references
    - $ 8.3 bn
  - EU
    - Energy crop payment: 45€/ha (max. € 90 mn)
    - Single farm payment (*ex* compensatory payments)
    - 2004: Cereals €11.9 bn and oilseeds €1.3 bn

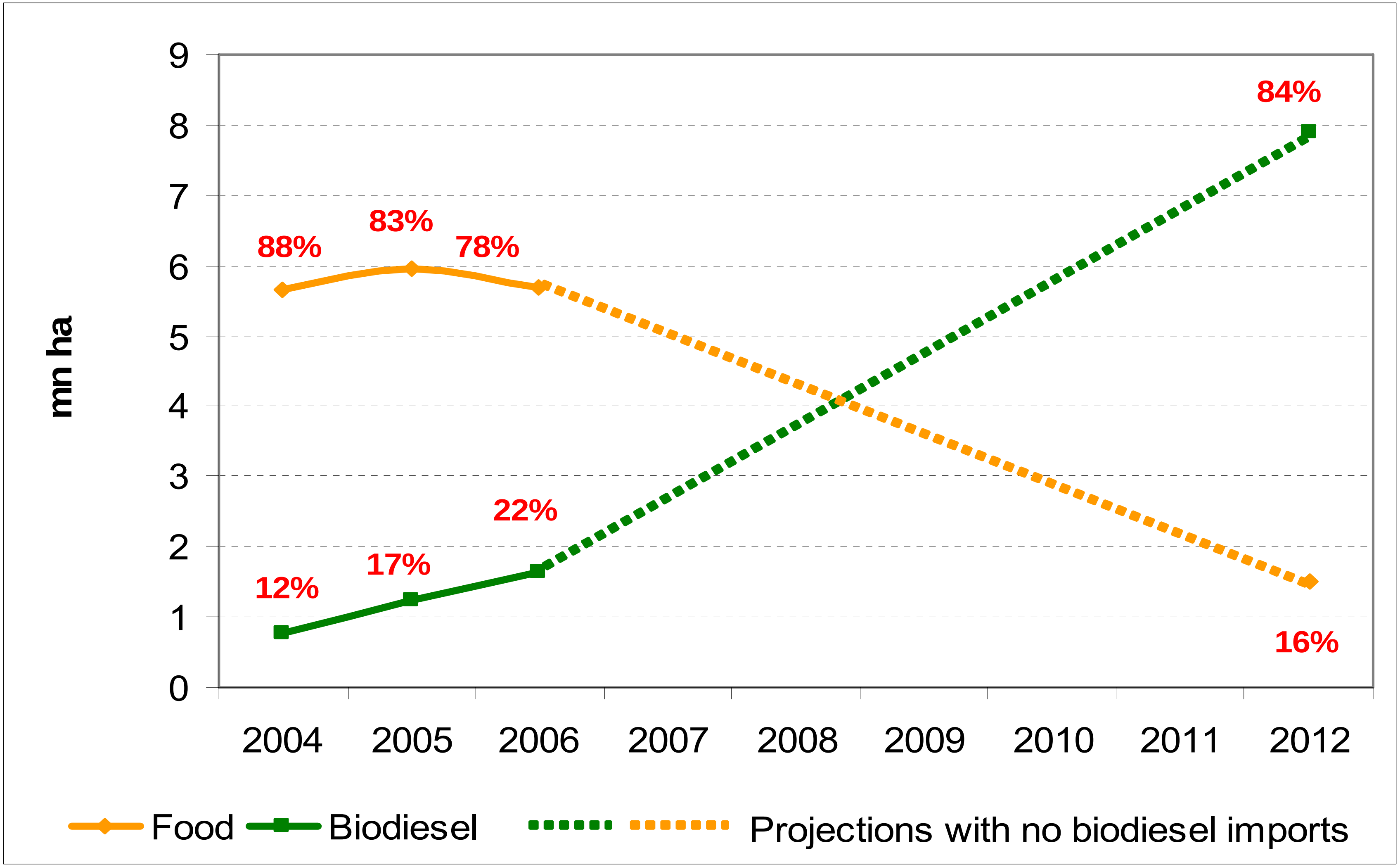
- Tax exemptions
  - US: 0.135 US$/liter on ethanol from all origins (+ 14¢/liter on imports)
  - EU: Tax exemptions apply only to approved operators in countries with quotas, so imports are excluded from this scheme (Belgium, France, Ireland, Italy)

Other barriers

- Local content requirements
  - Louisiana and Montana
- EU technical norms on biodiesel
  - Limit the incorporation of soy oil and palm oil into biodiesel.
- Toward the application of sustainability standards in the EU?
- Etc.

Drivers that could foster biofuels imports in developed countries

European Union: Insufficient land availability for biodiesel feedstock



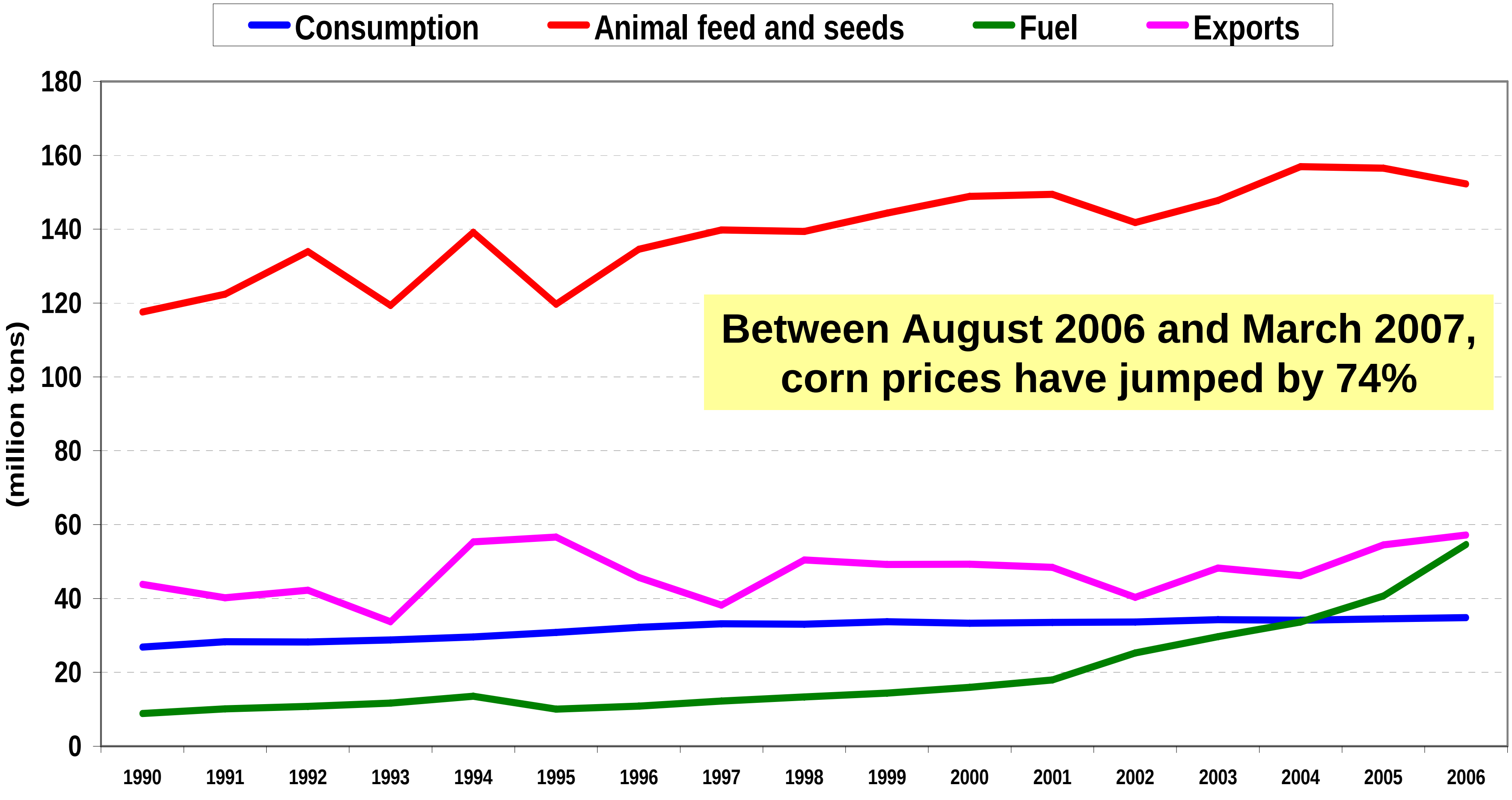
Source: GEM

European Union

- Pressure on rape oil prices will become unsustainable
  - ► EU will have to import biodiesel and/or vegetable oil
  - ►By 2012, EU imports of biodiesel/vegetable oil could reach 4.16 mn tons (50% of oilseed areas dedicated to feedstock for biodiesel)
- Costs for taxpayers and governments are very high

- Areas for ethanol production are not an issue in the medium run, **BUT**
- ACP agreement (0% tariff) and financial compensation for decrease of sugar prices sugar
- EU countries not be able to produce their own biofuels or not willing to bear the high costs of locally produced biofuels (Exemple: Sweden)

US: Unsustainable pressure on corn utilization and prices



Source: ICONE

The United States

- The US current production of corn could only displace 15% of gasoline consumption
- Current RFS target: 28.4 bn liters by 2012
- Planned capacity 2012: ~ 41.7 bn liters (7.4% of gasoline)
  - ► If the target is not moved: imports will depend on the export potential of countries with preferential access to US market.
  - ► If the target increases: US will have to import from other countries such as Brazil.
- Excise tax credit should represent a loss of \$ 2.2 bn per year (2006-2010) → Very costly

Limitations on the export potential of developing countries

Ethanol

- For many developing countries, access to the US and EU markets is not a problem
- Limiting factors:
  - Production capacity and competitiveness
  - The decision to engage in an ambitious bioethanol program depends on:
    - Potential for sugar expansion (areas/yields);
    - Capacity to attract investment will depend on the development of a domestic market and incentives provided by national governments. The positive evolution of demand in the EU and US can be a strong driver for this expansion of production capacity in developing countries;
    - Sugar policies in developing countries should be reformed.

Biodiesel

- Access is not the problem: tariffs are low
- Limiting factors:
  - EU standards (should be revised soon)
  - Potential negative effects of increasing palm oil demand:
    - Deforestation and effect on peats land
    - Price increase for local population
    - Palm oil as a substitute for human consumption?
  - Palm and soy oil present higher price sensitivity in response to biofuels demand increase because expansion possibilities are much more limited than for cane sugar.

Conclusions

- The development of ambitious and cost-efficient biofuels programs in developed and in developing countries is intimately linked to the potential expansion of feedstock production and to its impact on the production structures of the producing countries and on global agricultural markets.

- Developed countries: the expansion of import opportunities will reduce the upward pressure on feedstock prices and on biofuels prices, benefiting consumers and fostering biofuels consumption. In addition, the diversification of sourcing will minimize the risk of market disruptions.

- To facilitate imports that will complement domestic production and that could provide some relief on rising prices and budgetary pressure, developed countries should consider several options such as tariff reduction, implementation of tariffs associated with oil or feedstock prices, opening of a quota based on national consumption,…

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Thank you for your attention

European Biofuels Policy Research Program (EBP)

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