

STATE OF THE ARGENTINE BIODIESEL INDUSTRY

First Semester 2009 Report:

*International production rankings, increasing production levels,
and ongoing international commercial disputes*

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Este documento también está disponible en español bajo el título, *Estado de la industria argentina de biodiesel: Reporte del primer semestre 2009*, en www.argentinarenovables.org.

Summary

- In the last few months the Argentine biodiesel industry has stabilized output, if not profitability, and in August 2009 produced some 109,000 tons after a very good July;
- Our Chamber has discovered that the government database used to report monthly export figures, coming from the federal tax authority, has minor errors. Historical figures were in reality approximately 10% lower than initially reported;
- The price of biodiesel fob port of Rosario, Argentina, seems to have stabilized just below US\$800/ton in recent months;
- The federal government's long delays in reimbursing value-added taxes (VAT) to biodiesel exporters is damaging the industry – especially the smaller producers without access to working capital financing;
- The Argentine biodiesel industry is evolving into one with three distinct segments, each with its own interests, strengths and weaknesses;
- Argentina is the fifth largest biodiesel producer in the world, its place being taken by Brazil, now fourth largest producer;
- We estimate that Argentine biodiesel production in 2009 will reach 1.2 million tons, representing 10% of world supply, and will remain the fifth largest producer. US production is falling significantly in 2009 and will drop in rankings from second to third or even fourth largest producer;
- Trade conflicts with Europe continue to worsen, primarily because of a lack of understanding on the functioning of the Argentine industry by Europeans.

Introduction

In *The State of the Argentine Biodiesel Industry*, published by our chamber in October 2008, we established the groundbreaking analysis of the basics of the industry. Our follow-up study dated April 2009, *State of the Argentine Biodiesel Industry: First Quarter 2009 Report*, informed how the industry ended 2008 and provided insights into emerging international trade conflicts with the European Union as well as proposals to improve the Argentine domestic biodiesel market, which doesn't begin until January 2010. Both of the studies are available free of charge at www.ArgentinaRenovables.org.

These studies – also published in Spanish – were very well received internationally, and our institution has undertaken to report regularly in this *State of the Industry* series to allow the global community to also keep the pulse of developments and the issues that affect its development. This is particularly important since, as pointed out in this report, there seems to be an overseas movement to cause harm to our biodiesel industry. Any failure to disclose errors on our part, any evidence of disunity on our part, can be counted upon to be used against the Argentine industry to destabilize it.

The global biodiesel industry continues to evolve rapidly. European production seems to be shifting towards Eastern Europe (closer to its feedstock, rapeseed/canola); the U.S. industry appears headed to a contraction of as much as 40% this year and likely to drop in world rankings from second to perhaps fourth largest producer. Meanwhile, Latin American production continues to grow: Brazil has emerged as the fourth largest producer before even beginning to consider export markets; Colombia's production is exploding this year and may well appear among the world's ten largest producers for the year; and Argentina's production has returned to stability and is producing solidly once again. About a third of its production will be re-directed to the domestic market in 2010, but this is unlikely to significantly change the fortunes of the seriously over-built European industry. We're hoping they become more contemplative rather than continue to lash out at those with better fundamentals and long term prospects.

But at the same time one can see the beginnings of a massive shift toward second and third generation biodiesel, which will undoubtedly affect Argentina and its strong natural advantage in first generation oils.¹ Each country continues to organize and produce according to its capacities and competitive advantages, and one of the big news in this report is the revelation that Brazil has surpassed Argentina in biodiesel production, using the credibility, consistency, and ability for teamwork that they have already established in their very powerful sugarcane-based ethanol industry.

Argentina is slowly getting organized for the legally-mandated B5 requirement that begins in January 2010; we are pleased to see that some of the proposals from the government are along lines of what our Chamber has been proposing for months. Our Chamber, now with over 90 members² representing the entire value chain of the biodiesel industry (including producers), continues to push for far more transparency than currently exists from the public sector.

¹ For a detailed explanation of the difference between generations (in Spanish only, unfortunately), see *La Argentina y los biocombustibles de segunda y tercera generación*, published in July 2009 and available on our Chamber's website at: http://www.argentinarenovables.org/informes_estudios_ensayos.php

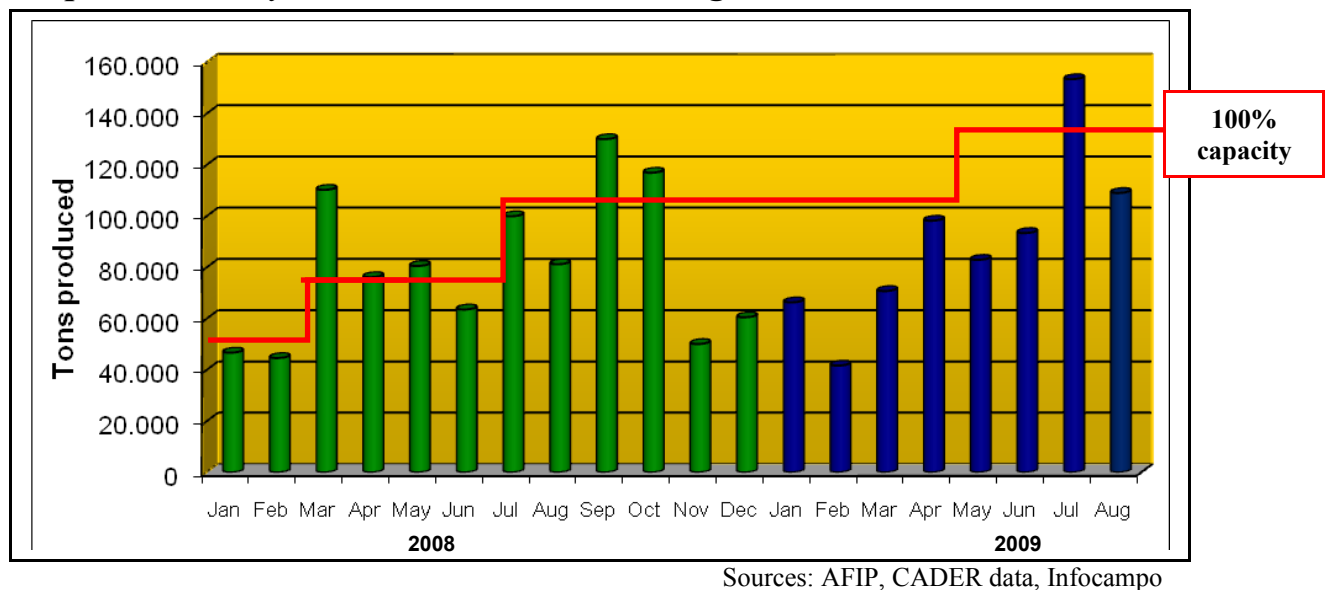
² Our member list can be seen here: www.argentinarenovables.org/miembros.php

Biodiesel Production in the first half of 2009

During the second quarter 2009, the Argentine biodiesel industry returned to some semblance of stability and in July even had very strong production levels.

As seen below in Graph 1, the industry's production fell sharply in the last quarter of 2008, reflecting the global economic slowdown and a sharp drop in biodiesel prices (see Graph 2, page 6). Since then it has been struggling to return to capacity, and in July it can be said this was achieved, with an estimated production of 153,000 tons, a significant jump from June, which we estimate at 93,000 tons. August 2009 production was about 109,000 tons.

Graph 1: Monthly Biodiesel Production in Argentina, 2008-2009



The July production figure appears extraordinarily high but can be explained away in two ways:

- Some 23,000 tons of July's production of 153,000 tons were shipped in the first three days of the month. This clearly represents June production.
- A biodiesel plant's nameplate capacity can vary considerably according to the efficiency with which it is operated. A plant can easily produce 10% more (or 10% less) working at full capacity. This also complicates the ability to correctly measure an industry's potential. Argentina's industry is primarily comprised of large plants that use internationally-recognized brand name technology, and uses almost exclusively soy oil as feedstock; it should not surprise that it can achieve great efficiencies in production.

In addition to these two reasons, there is a third: seasonality. Demand for soy-based biodiesel (SME) is higher during the European summer. These consumption patterns affect feedstock usage, and SME is preferred in summer. Use of palm oil-based biodiesel (PME, exported from countries such as Malaysia) is falling in Europe and used only in the hottest months (July-August) because at low temperatures it tends to gel. Additionally, Europe is trending away from PME claiming sustainability and quality concerns; some large oil companies have already made the decision to prohibit its use – which gives Argentine SME an additional advantage. In winter, Europe uses primarily locally grown Rapeseed Methyl Esther (RME).

Discrepancies in the Reported Monthly Production Figures

The data that our Chamber uses to analyze Argentine production levels comes primarily from the government: the Federal Public Revenue Administration (*Administración Federal de Ingresos Públicos*, or “AFIP”). AFIP has an open website allowing anyone can track exports and imports and see taxes on products and services.³ However, in recent months we realized that these figures are sometimes inaccurate; we found that exports are double-counted in some instances. Biodiesel export data first enters the government database when an exporter informs of its intent to ship. However, on occasion these shipments are delayed (or simply do not occur) for any number of reasons, and then get registered a second time when they re-register to ship without the first one being taken off. Therefore, before having caught this error, our industry figures were higher than the actual figures. We regret any inconvenience this may have caused.

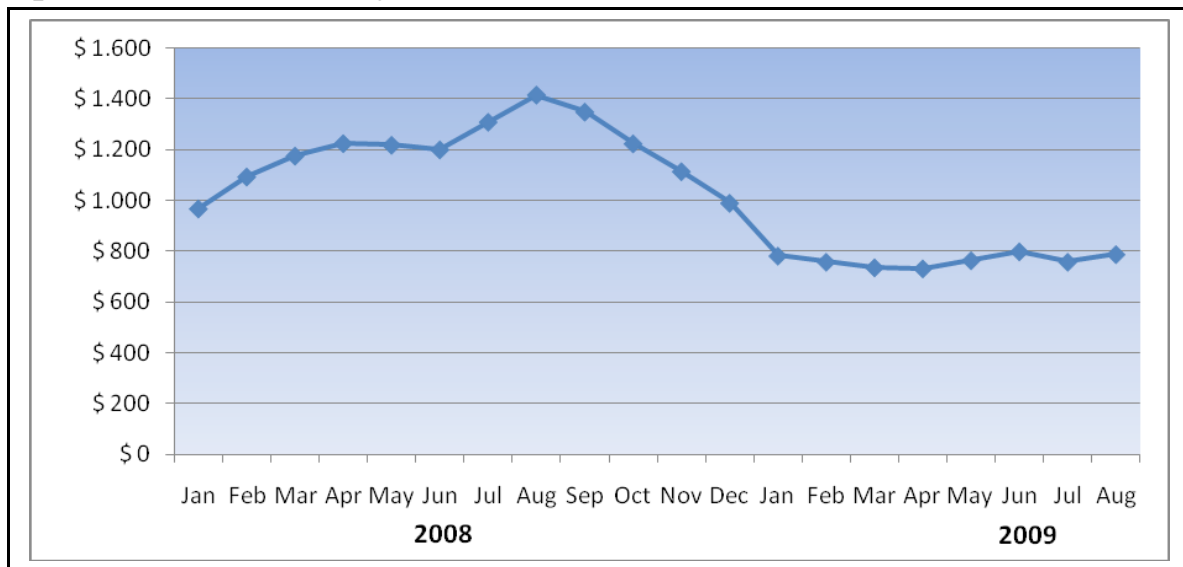
Our institution is seeking ways to get more accurate figures, but until then a quick review indicates that about 10% of figures were over-counted; so until further notice we believe that a 10% across-the-board reduction will more accurately represent the industry’s production levels for each month. In addition to this we will also inform that our figures may vary within a certain range. This is not an uncommon practice: the production figures for Europe, available on the European Biodiesel Board’s website, announce that their figures have a margin or error of +/- 5%; in our case we will do the same, indicating that figures may vary within a +/- 10% range.

Biodiesel prices from the port of Rosario, province of Santa Fe, Argentina, seem to have found some stability, remaining below US\$800/ton on average since beginning of the year. (see Graph 2, next page).

These prices – when coupled with the exorbitant taxes Argentine biodiesel pays -- continue to punish the industry. Only the most efficient are able to cover all costs. In the last month individual transaction prices fluctuated between US\$660/ton and US\$878/ton; this 33% range has also been fairly consistent in the last few months (this information is also available on the AFIP website). Adding further pain, the Argentine government’s decision to slow down – if not altogether halt – Value-Added Tax (VAT) reimbursements are also aggravating the industry’s ability to operate profitably.

³ The ID number for biodiesel is known as a *Posición Arancelaria* (“PA”); it is 3824.90.29.100P. The page is: <http://www.afip.gov.ar/aduana/sim/Default.asp?tipo=E>

Graph 2: Biodiesel Prices job Rosario, US\$/ton



Sources: AFIP, data CADER

Delays in VAT Reimbursements Causing Havoc with Producers

A new concern for biodiesel exporters is the virtual cessation of VAT (Value-Added Tax, not unlike a sales tax) reimbursements by the federal government since about November of last year. This is an important impediment to the sound workings of the industry, since it negatively affects producers – especially the smaller ones who have little liquidity to begin with and no access to bank financing.

When a producer buys the raw materials to make biodiesel, it pays the corresponding VAT;⁴ once the final product has been exported, the government is obliged to reimburse this tax to the producer. Given the high level of taxes in Argentina, the numbers are large: for a small producer, for example, who must buy soy oil, methanol, caustic soda, antioxidants and other materials, this can easily total some US\$2 million per month. The corresponding VAT on this is about US\$400,000/month. A large producer has many times this figure to finance.

A recent study by the Union Bank of Switzerland does an excellent job of explaining the reality behind these issues.⁵ Table A below shows the numbers: government revenues *appear* to have increased 15% during the first semester of 2009 (compared to the same 2008 semester). But this is due to three specific issues, among them the lack of VAT reimbursements:

⁴ The value added tax in Argentina is 21%.

⁵ *Argentina: Lack of Financing to Force a Market Friendlier Agenda*, Javier Kulesz, July 17, 2009, UBS Investment Research, www.ubs.com/economics

Table A: VAT Reimbursements and Government Tax Revenues

Table 1: Tax revenue collection Jan-Jun (ARS millions)

	2009	2008	% change
Income tax	26,986	25,764	5%
VAT	41,061	38,322	7%
Reimbursements	2185	4,315	-49%
Social security	35,704	22,972	55% ★
Financial transaction tax	9,739	9,178	6%
Energy	5,038	4,617	9%
Export taxes	15,943	16,455	-3% ★
Import tariffs	3,474	4,309	-19%
Asset tax	2,263	2,031	11%
Others	5,534	3,495	58%
Total	145,742	127,143	15% ★

Source: Mecon

Source: UBS Investment Research

1. An apparent increase in pension fund payments of 55% is in reality the result of the nationalization of all pension funds in December 2008;
2. The drop in export tax revenues collection appears to have fallen only 3%. However, as Javier Kulesz points out in his study, it parts from an exceptionally low base in 2008 when the farm crisis (due to attempts to increase export taxes further) resulted in a significant drop in exports in 2008; and
3. A significant drop in VAT reimbursements. It is marked in the red box above and shows a 49% decline when compared to the first semester of 2008. The difference of \$2.1 billion pesos (about US\$600 million) represents funds belonging to exporters and owed by the Argentine government.

In a country with virtually no bank financing, this reality crushes any exporter – in particular the smaller ones.

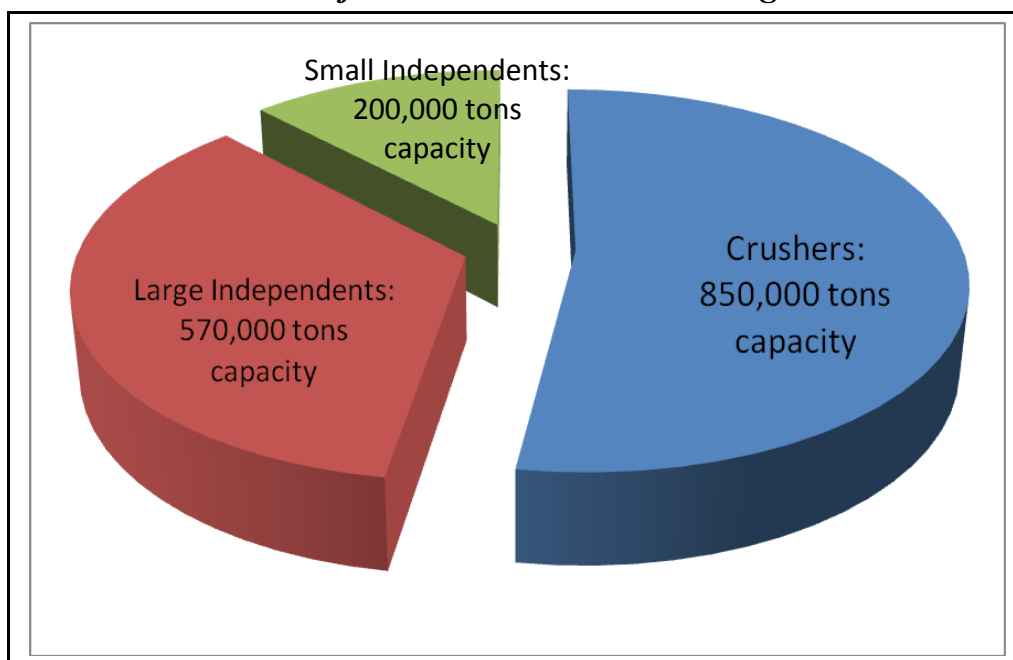
The Three Emerging Castes of Producers

The Argentine biodiesel industry is evolving into one with three classes or castes of producers, each with special conditions that differentiate them from the others. While in some cases the lines between them can be blurred, there is no doubt that there are significant differences between these market participants and this segmentation may prove a way to better understand them. To the extent that the industry understands the interests, strengths and weaknesses of each group, we will be in a better position to structure the industry more efficiently.

The most successful are the **large oilseed crushers** with their own equally large adjacent biodiesel plants: strategically located on ports, with excellent access to working capital, high levels of professionalism and international networks of offices and production facilities. But above all, with access to an abundance of feedstock: soy oil. Among this group we find the biodiesel plants of Vicentin; Renova (a JV between Vicentin and Glencore); Ecofuel (Aceitera General Dehesa and Bunge); LDC Argentina (Dreyfus); and Rio Molinos de la Plata. The installed capacity of this elite group is about 850,000 tons/year and it is working at full throttle again.

The **second class** of producers is comprised of large plants that are not directly associated with any of the oilseed crushers. They have strong financial backers, excellent production facilities (like the above, typically foreign brand technology), and are well located near ports, but have the drawback of having to buy feedstock from the above crushers. Some have sought to develop their own second generation feedstock to reduce this dependency with mixed success, but these plants are increasingly working under arrangements that look like variations of tolling for the neighboring oilseed crushers. Among these are enterprises such as Unitec Bio, Explora and Patagonia Bioenergía. The installed capacity of this group is about 570,000 tons/year. This segment is working well but not as consistently as the first caste. Some of these have signed long term supply contracts with crushers, which makes them a hybrid of the first two castes.

Graph 3: The Three Castes of Biodiesel Producers in Argentina



Source: CADER

The **third class** is the one that is suffering the most and belongs to those with small to medium-sized facilities. They are typically built with Argentine technology (many of them of excellent quality and far more affordable), but are often located far from both ports and access to feedstock, and as small enterprises do not have ready access to working capital lines of credit to survive the timing required for an export – even less with the long delays in VAT reimbursements explained above. This group has suffered the most in the last year and it is here where one is more likely to find closed plants. The more fortunate ones work under a tolling

arrangement for a large crusher, with tight margins, or find direct overseas clients with no middlemen. Our Chamber has helped some of these producers to find overseas customers. Among this group are companies such as Soyenergy, Biomadero, Derivados San Luis, Pitey, and Energías Renovables Argentinas, among others. The installed capacity of this group is approximately 200,000 tons/year.

It is this last group, the Small Independents, which need the most help and whom biofuels law #26.093 is meant to protect. But this segment may also show the most growth in the coming years by focusing on the upcoming domestic market, since the other two groups have many of their expansion projects on standby given their slim margins, the unstable world economy and the ongoing commercial conflicts with Europe and now the United States as well.

The Argentine government's vision is one with a large expansion of medium-sized plants⁶ geographically distributed throughout the country; while less efficient from an economic standpoint than a large plant, this structure allows for a greater source of jobs and distributes wealth creation more equitably to entrepreneurs. The fact is that the second and third castes (the "Independents") have more in common than the first and second, although it is understandable that the Large Independents (which we might also call the "middle class") might prefer to align itself with the big crushers. However, given the industry's evolution and ongoing complications in exporting product to Europe, the Large Independents may be better off positioning themselves as larger small and medium enterprises and seek to enter the domestic market as an interim solution. Note that the installed capacity of the Independents is approximately that needed to supply the B5 domestic market beginning in a few short months. (The Argentine B5 market is estimated at 700,000 tons/year, which will also have the effect of reducing the amount of biodiesel available for export beginning next year.)

Thus, in the same way that the Small Independents are ideal to supply the domestic market and the Crushers are best positioned to export, the Large Independents in between are an ideal "pressure valve", fluctuating between exports and domestic market while the politics behind the domestic market are resolved.

Slow Progress on Establishment of the Domestic Biodiesel Market

And there is no shortage of politics. It is clear that the domestic market, which under the biofuels law requires plants that are approved specifically and exclusively for that market,⁷ will not be able to begin as established by law: not a single plant has sought approval for the domestic market and all plants are only authorized to export (see Table B, below). While this may appear to be because of the attractiveness of export opportunities, the reality is that exporters are less regulated and operate in a relatively free market environment, whereby those choosing the domestic market option are over-regulated, have to accept government intervention on pricing and considerable restrictions on shareholder rights. Our Chamber recently completed an analysis of Argentina's biofuels policy and legal framework in English as part of its work in the European Commission-funded "BioTop" project which provides greater depth of understanding to the country's legal framework.⁸

⁶ The Application Authority extra officially envisions plants with an average capacity of 50,000 tons/year each.

⁷ This is because domestic producers will enjoy tax benefits and exporters have been given none.

⁸ See *Biofuels Policy in Argentina* at www.argentinarenovables.org/archivos/ArgentineBiofuelsPolicyJune2009.pdf

But we are pleased to note that the government is beginning to meet with all producers (i.e., exporters) to seek solutions, and we are pleased to report that many of their proposals were taken from our recommendations in previous studies.

Argentine biodiesel producers are only allowed to export at present. However, while the internal market mechanisms are being defined and biofuels law #26.093 begins to approximate its potential, we continue to insist that existing producers should have the option – but not the obligation – to offer their product to the domestic market, as long as the Small Independents receive favorable treatment as suggested by the spirit of the law. This is something that the rest of the world has managed, including Brazil, whose average plant size is far smaller than that of Argentina.

Table B: Biodiesel Plants Formally Authorized by the Government to Export

1	Vicentin S.A.
2	Energía Sanluisiense Refinería Argentina S.A.
3	Soyenergy S.A.
4	Advanced Organic Materials S.A.
5	Biomadero S.A.
6	Renova S.A.
7	Ecofuel S.A.
8	Unitec Bio S.A.
9	L.D.C. Argentina S.A.
10	Molinos Rio de la Plata S.A.
11	Explora S.A.
12	Patagonia Bioenergía S.A.
13	Ecopor S.A.
14	Energías Renovables Argentinas S.R.L.

Source: Secretaría de Energía, as of September 6, 2009

Our Chamber is also completing an analysis of the Brazilian biodiesel market mechanics (Brazil does not export at all; the entirety of its production is consumed domestically). It operates through a series of open and transparent monthly and quarterly bids, traits that the Argentine system could well emulate. Last quarter's winning biodiesel bids for sales ex-works to Petrobras were for the equivalent of US\$900/ton -- while international market prices were closer to US\$800/ton. This study will be available on our website in the coming weeks. However, exports to Brazil are closed: a recent Argentine shipment that attempted to slip through resulted in confiscation of the biodiesel and heavy fines.

Please note that all of these studies will soon be available free of charge only to members of our Chamber.

World Biodiesel Production Rankings

Europe is still the continent with the greatest biodiesel production, although the rise of Latin America – specifically Brazil, Argentina and beginning this year, Colombia – is an indicator that as long as first generation biofuels dominate the market, our region appears headed to lead in world production.

The European Biodiesel Board (EBB) recently published its list of production by country for 2008, and some trends are visible. For example, Germany maintained its leadership, although total production declined 3% (see Table D with 2008 figures). Spain's production also increased, but comparatively little, and given the rise of production in countries like Brazil, Argentina and Poland, has now dropped out of the Top Ten. Also, there seems to be a migration of production from Western to Eastern Europe, where the majority of feedstock (rapeseed/canola) is grown: note the growth rates of countries like Poland, Slovakia, Hungary, and the Czech Republic. But note also that Germany and Spain are the two countries with the biggest over-capacity and those asking the European Commission to sanction Argentine biodiesel.

But the big news is that Brazil is already a bigger producer of biodiesel than Argentina. Brazil's leadership in sugarcane-based ethanol is already well known, and Brazil's national energy agency (*Agencia Nacional de Petróleo, Gas Natural y Biocombustibles*, or "ANP") recently completed an analysis of their own industry which shows that in both 2007 and 2008 Brazil produced more biodiesel than Argentina. Since the entirety of Brazilian biodiesel is consumed domestically, it was below the global radar screen.

Thus, since the industry came to life, Brazil has been a bigger producer than Argentina, which goes in line with world soy production figures: in 2008, the U.S. harvested almost 73 million tons of soy, followed by Brazil with 61 million tons. The third place is held by Argentina with 46 million tons, followed by China with 14 million tons.⁹

We include in Table C the list of 2007 producers for comparison. Note the appearance of Malaysia as a strong producer in 2007, remaining in the Top Ten in 2008 despite a noticeable slowdown in growth. According to data from the *Department of Statistics, Kuala Lumpur*, practically the entirety of Malaysian production is exported. In 2008, half was shipped to Europe (entering through the Netherlands), a quarter sold to the US, and remainder to mostly Asian countries.

We also include figures for Colombia of about 23,000 tons in 2008, as well as Indonesia with some 80,000 tons. Colombian production is set to explode in 2009 and may even end the year among the Top Ten if plant startups go well.¹⁰ Also, Indonesia, with more than five times the area of its neighbor Malaysia, is a country to watch. Other noteworthy changes in 2009 include the United States, whose production is expected to fall by as much as 40% to approximately 1.4 million tons during 2009 according to figures from the National Biodiesel Board, and may well lose its second place ranking.

⁹ Source: www.soystats.com

¹⁰ We thank the support and research of Dr. Jorge Bendeck, Executive President of the *Federación Nacional de Biocombustibles de Colombia*, see also www.fedebiocombustibles.com

Table C: World Biodiesel Production Rankings¹¹ in 2007

Rank	Country	Production*
1	Germany	2,890
2	USA	1,521
3	France	872
4	Malaysia	400
5	Italy	363
6	Brazil	356
7	Austria	267
8	ARGENTINA	180
9	Portugal	175
10	Spain	168

* in thousands of tons

Table D: World Biodiesel Production Rankings¹² in 2008

Rank	Country	Production*	Change from 2007
1	Germany	2,819	-3%
2	USA	2,327	+53%
3	France	1,815	+108%
4	Brazil	1,027	+189%
5	ARGENTINA	960	+433%
6	Italy	595	+64%
7	Malaysia	420	+5%
8	Belgium	277	+67%
9	Poland	275	+244%
10	Portugal	268	+53%
11	Denmark/Sweden	231	+56%
12	Austria	213	-20%
13	Spain	207	+23%
14	UK	192	+28%
15	Slovakia	146	+217%
16	Greece	107	+7%
17	Hungary	105	+1500%
18	Czech Republic	104	+70%
...	Indonesia	80	-12%
...	Colombia	23	NA

*in thousands of tons

Source: Argentine Renewable Energies Chamber

¹¹ Sources: European Biodiesel Board; National Biodiesel Board (USA); ANP - Agencia Nacional de Petróleo, Gas Natural y Biocombustibles (Brazil); *Malaysia Biofuels Annual Report 2009* from USDA; *Indonesia Biofuels Annual Report 2009* from USDA. For *Argentina*: Administración Federal de Ingresos Públicos (AFIP), CADER, Infocampo, various producers. The EBB allows for a +/- 5% variance in its figures. Those from Argentina have a possible +/- 10% variation.

¹² Ibid

Globally, F.O. Licht recently estimated that world biodiesel production will remain constant at about 12.5 million tons (compared to 12.7 million tons in 2008). Yet at the same time installed capacity will rise by some 12% to 37.9 million tons (from 33.9 million in 2008). This foretells ongoing international strain and conflict in the industry.

It is important to note that all of the above countries established their biodiesel industries by focusing first on domestic markets and only later – if at all -- overseas. With two exceptions: Argentina and Malaysia. The only other country on the list that exports (or perhaps more accurately, exported) noticeable volumes is the United States. Each of these countries has trade conflicts with the European Union, largest consumer of biodiesel and with an increasing level of overcapacity coupled with a shortage of feedstock. *EurObserv'ER* recently published an analysis where it concludes that the EU will not be able to meet its target of 5.75% biodiesel due to insufficient production.

International Trade Conflicts

The European industry asks that Argentine biodiesel be “watched closely”

In our study of April 2009 we explained¹³ the nature of the conflict between Europe and Argentina in biodiesel. In summary, the focus is on greenhouse gas (GHG) reductions that result from using different feedstocks to produce biodiesel. Europe has established a floor of 35%, i.e., any biofuel entering Europe must reduce emissions by at least that amount when compared to a diesel benchmark. According to the European analysis, using palm oil to make biodiesel results in GHG reductions of 56%; using rapeseed/canola (as in Europe), 38%. These meet the new standards. Soy-based biodiesel, however, was given a GHG reduction of only 31%, insufficient to enter the European market without special certifications.¹⁴

Given that this certification requirement has not yet formally begun, the European biodiesel industry continues to suffer the effects of over-development borne of great enthusiasm to enter a new industry and with easy access to venture capital and financing, along with government-subsidized prices. However, they did not consider adequately their access to raw material nor competition from countries such as Argentina with large, efficient and very professional industries, as well as the critical component of being among the largest producers of feedstock.

The association that represents Europe's biodiesel industry, the European Biodiesel Board (EBB), recently asked the European Commission to “watch” Argentine biodiesel exports, presumably as a first step to establish trade barriers. Yet our investigations have found that more than a quarter of biodiesel produced in Europe still uses Latin American soy oil as feedstock.¹⁵ Apparently, Argentine soy biodiesel is not acceptable in Europe, yet Argentine soy oil is welcome.

The EBB has also asked the European Commission to investigate other market distortions that, according to them, also involve Argentina. As shown below, these too are without merit. In

¹³ See: *State of the Argentine Biodiesel Industry: First Quarter 2009 Report*, at <http://www.argentinarenovables.org/archivos/ArgentineBiodieselMarket09.pdf>

¹⁴ Studies from INTA as well as earlier US government studies show that GHG reductions using soy are actually closer to 73%.

¹⁵ *Soy consumption for feed and fuel in the European Union*, Profundo Economic Research, October 28, 2008, The Netherlands

2008 the European Commission fined some fifty U.S. companies involved in biodiesel trade for selling below market prices (we refer to what is known as “splash & dash”). With direct sales of biodiesel closed to these companies, the EBB suggests that US biodiesel is now being exported to countries such as Argentina and from there re-exported to Europe as Argentine production.

Biodiesel Imported to Argentina for Re-Export to Europe

However, if that were the case, Argentine production levels would appear significantly above installed capacity (see Graph 1, page 4). Also, the government website referred to earlier would also show biodiesel imports, if nothing else because absolutely everything is taxed in this country. Our Chamber contacted the EBB to offer our assistance in their investigations as we do not condone illegal triangulations of the type suggested, and to inform them of our intentions as well.

We found nine instances of biodiesel imports during calendar 2009, two of them from the United States. But in each instance, the product arrived by air and never exceeded 10 kilos (about 22 pounds), which belies them as samples. We also contacted the National Biodiesel Board in the U.S., who researched possible exports of U.S. biodiesel to Argentina and they also came up empty-handed. Therefore, we conclude that Argentina is not participating in some type of “reverse splash & dash” as suggested by Europe. We have sent this information to the EBB for their independent review. Our Chamber will continue to report Argentine monthly production figures showing the theoretical capacity limits to keep an eye on the matter and to show our commitment to fair trade.

Yet the level of misunderstanding within Europe is noteworthy. No less than the CEO of Verbio AG, one of the world’s largest biodiesel producers and a company that is listed on the European stock exchange, recently made comments in an interview that appears on the Bloomberg website that include statements such as that there is “no export tax” on Argentine biodiesel (in reality, it pays an astounding 20% in export taxes), and that Argentine biodiesel enters Europe, “mainly to the UK and Spain”¹⁶ (in reality, almost the entirety of Argentine biodiesel enters through the Netherlands; none of it through the UK, and in July, for example, only 6% entered through Spanish ports). We communicated with Bloomberg to ask for them to correct this information but they chose not to do so.

Another example of this misunderstanding comes from the Swiss-German biodiesel producer Biopetrol, which also recently asked the European Commission to investigate “subsidized” imports from Argentina, which were incorrectly compared to those from the United States. The difference is an important one: in the U.S., traders found loopholes in specific tax incentives created for the biodiesel industry; this is not the case in Argentina.

It is important to insist once again that Argentine biodiesel exporters do not enjoy direct subsidies or fiscal incentives. The text of the biofuels law and its regulations are available on our Chamber’s website so that anyone can see what is offered to an exporter: virtually nothing. Quite the contrary: they pay an extraordinarily high export tax of 20%¹⁷ (perhaps one of very few countries in the world that taxes biodiesel exports). In addition to this they must pay an

¹⁶ See <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=amt9qomfTNZO>, of August 18, 2009.

¹⁷ The government allows for a 2.5% reimbursement of the export tax under certain conditions.

income tax of 35%. This reality, coupled with un-reimbursed 21% valued-added tax outlays makes for an industry with difficulty in earning profits.

It is difficult to understand how European biodiesel producers can accuse the Argentine industry of having unfair trade advantages or suggest it is involved in underhanded trade schemes when it is relatively easy to know the truth.

The Argentine Tax Structure comes from Classical Economic Development Theory

Europeans note the differential in export taxes (known locally as “*retenciones*”) between soy oil (a 32% tax) and biodiesel (20% tax), alleging that this differential represents an indirect subsidy to biodiesel. The Argentine system of export taxes is one borne from classic development economic theory, seeking to drive investment towards value-added products in the country. Thus, in the case of Argentina, soybean exports are taxed at 36%. If an investor builds a crushing facility, the tax on soy oil is lowered to 32%. And if an investor further adds to the value chain by building a biodiesel plant, the tax falls to 20%. This is a very simple way to create investment incentives that generate more complex and high-paying jobs and national wealth instead of following the model of an under-developed country selling only beans to Europe so all value added can be done overseas. It is important to note also that studies have shown that Argentina dedicates an area larger than the size of Switzerland just to grow food for European livestock.¹⁸

But in the end, it is still an additional tax of 20%, not a subsidy.

New Challenge from the U.S. Environmental Protection Agency

In May of this year the U.S. Environmental protection Agency (EPA) announced concrete plans to increase biofuel production from some 11 billion gallons in 2009 to over 35 billion gallons (equivalent to 132 billion liters, or 116 million tons of biodiesel, for example) by 2022. (For comparison and to see the magnitude of the potential of the U.S. market, the combined 2008 production of the Top Ten biodiesel countries did not reach 11 million tons.) The greatest growth will come from third generation technologies, using cellulosic material to make the biofuels of the future. They also seek to lower GHG emissions and the EPA has raised the bar even higher: while the EU requires a minimum GHG reduction of 35%, the Americans have drawn the line much higher, seeking reductions of 50% -- and in some cases 60%.

The focus of the Obama government is to find second and third generation solutions. And part of the process of creating incentives to develop new solutions is to begin closing the doors on first generation technology, which adversely affects Argentina. Not so much because we export to the U.S. (as a matter of fact very little is exported to the U.S. market) but because the EPA’s studies come with a number of misconceptions regarding soy-based biodiesel, for example, and doesn’t take into account sufficiently the fact that for the medium to long term, few feedstocks have the abundance and versatility of soy.

A summary (in Spanish) with graphs of the EPA’s proposals can be found on our Chamber’s website on the Studies and Essays page under the name, *Resumen de las propuestas recientes de*

¹⁸ See *State of the Argentine Biodiesel Industry: First Quarter 2009 Report*, page 12.

la Agencia de Protección Ambiental de los EEUU y su posible efecto a la industria argentina de biodiesel, in powerpoint, published in May 2009.¹⁹

Here two local institutions have taken leadership of the issue: the National Institute for Agropecuary Technology (*Instituto Nacional de Tecnología Agropecuaria*, or INTA) as well as the Argentine Corn and Sorghum Association (*Asociación de Maíz y Sorgo Argentino*, or MAIZAR). These two organizations, this first one a government agency, have brought together most of the actors in the industry to develop a common front. Our organization also supports their initiative and is working closely with them.²⁰

In the mean time, our Chamber is also looking for ways to work with the U.S. and Brazilian biodiesel industries – also soy-based – to jointly take on these challenges. Between our three countries we represent more than a third of world biodiesel production. This fact, plus our Chamber's role as member of the Global Renewable Fuels Alliance, can add up to significant influence on the global stage.

Conclusion

The global biofuels industry is rapidly evolving towards second and third generation. As indicated in other publications from our chamber, Argentina holds great promise in successfully developing second generation solutions such as jatropha, algae or camelina, but not in third generation solutions that are technology-driven. The unknown factor is how this evolution might affect the interest of the large crushers (the first caste) in remaining in the industry in Argentina. These will have to decide if they really want to become energy enterprises or if they return to their longstanding roots (and profit centers) within the agro industrial sector. This could well open new doors to the second and third castes, and this is where the future of the Argentine bioenergy industry lies.

In a few months the B5 domestic market opens. This new legislatively-created market will generate the equivalent of more than US\$500 million in revenues to producers. Yet the government not only decides who participates in the domestic market but also determines the industry's profitability.²¹

We would like to propose a more transparent mechanism.

As explained in our groundbreaking study of October 2008, the work before the Application Authority (i.e., the Secretariat of Energy) is enormous, and those in the public sector deserve our respect for the gains achieved by the industry thus far. They have worked hard, creating a legal framework out of nothing in a new industry, with insufficient human resources or leadership (the Secretariat of Energy continues without a formally designated Undersecretary of Fuels, a position that has been vacant for over a year), and under considerable pressure from the private sector (including our own Chamber) to resolve and clarify the thousand and one pending issues needed for the orderly working of an industry.

¹⁹ See <http://www.argentinarenovables.org/archivos/EPAsummary.pdf>

²⁰ Special mention is made to the work of Ing. Jorge Hilbert of INTA and Ing. Martín Fraguio from MAIZAR.

²¹ See biofuels law 26.093, for example, Article 4, (l), (n), y (r). Text of this law can be found (Spanish only) on the Chamber's website: www.argentinarenovables.org/leyes.php

But our Chamber was founded because our members see in the renewable energies industry a unique opportunity for Argentina, which can become once again something that it once was: a wealthy nation, internationally admired, an undisputed regional leader and with a solid middle class.²² We have lost every one of those traits; that Argentina no longer exists, but the potential we to develop biofuels, as well as wind, solar, geothermal, tide and other energies, put the country in a unique situation to return to the right path. It represents in large measure the best of our country's potential.

Our members believe in the importance of having a transparent and efficient industry; we seek to have it grow in a healthy manner. Self-regulation is unheard of in Argentina, yet we propose that this option be considered seriously. There is no better way to force an industry to grow up than to make it take responsibility for itself.

As a first step we seek that the private sector be allowed to participate more actively in the process of plant approvals, leaving aside structures that concentrate the decision-making process in the hands of very few with little oversight and thus inviting mistrust. We suggest creating public-private committees for this purpose. Biofuels legislation allows for something like this and it is contemplated in Article 3(g) of decree 109/2007, where the Application Authority must "arbitrate a procedure for the selection of projects".

Argentina is already among the five largest biodiesel producers and the world is watching us closely to highlight any mistake or inconsistency on our part. This is our laboratory.

Let's not mess this one up.

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²² On youtube.com there is an old documentary in English produced by Metro-Goldwyn-Mayer in 1932 which gives a glimpse of the respect and admiration the world had for Argentina, entitled, "*Romantic Argentina*". Ten minute short clip. See it at: <http://www.youtube.com/watch?v=O2Bvvt7sUA4&feature=channel>



About the Argentine Renewable Energies Chamber and the Author

The Argentine Renewable Energies Chamber (“*Cámara Argentina de Energías Renovables*”, or CADER) is a non-profit industry trade organization dedicated to promoting the sustainable development of alternative energies in our country. Our mission is to protect the interests of its members, pushing for the establishment and development of a vibrant and respected industry, respected globally and with the highest standards, practices and focus.

The first requirement to achieve this development is providing access to accurate information. Thus, CADER publishes on a regular basis studies in different sectors of the renewable energies industry in Argentina, describing fairly its state and opining on areas that need further improvement, with a goal of becoming an attractive investment center on a global basis.

This mindset has already paid dividends: our institution has been invited to become a board member of the recently established Global Renewable Fuels Alliance, a worldwide non-profit industry association based in Toronto, Canada that represents over 60% of global biofuels production in 30 countries. Our goal in this organization is to help in the development of a strong industry globally with fair trade practices and accurate information.

This last point is especially part of CADER’s philosophy since inception: to help Argentina establish a position as a global player in renewable energies and one of its leaders.

For more information, please visit our website at www.ArgentinaRenovables.org, write us at info@cader.org.ar, or visit our offices at Viamonte 524, Suite 101, Buenos Aires, C1053ABL, Argentina.

About the Author

Carlos St. James is the founder and chairman of the Chamber and works in the private sector as a consultant to the industry. He has been a speaker at renewable energies conferences in Argentina, Austria, Brazil, Canada, Chile, the Czech Republic, Germany, Mexico, Paraguay, Peru and the U.S., sought for his vision of the industry and knowledge of commercial and legal aspects of biofuels in Latin America. He is the author of a number of studies on the biofuels industry and board member of a number of institutions focused on renewable energies in Europe, the U.S. and Argentina. For more details about Mr. St. James and his upcoming speaking engagements, please see www.santiagosinclair.com/StJamesBio.html.