

South America Ethanol

Brazilians want fair cut

Tariff extension on imports presents the 'one true barrier' to the lucrative US market

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Brazilian ethanol exports to the US have slumped, and are expected to drop steeply again this year. The cause? The US Farm Bill, which took effect in October.

The bill extended a tariff on ethanol imports that was introduced in the early 1980s. It also eliminated a duty drawback that had in effect cancelled out the impact of the tariff.

The Food, Conservation and Energy Act of 2008, as the Farm Bill is formally known, extended a \$0.54-a-gallon tariff on Brazilian ethanol until the end of 2010. Producers are lobbying against the stiffening of the tariff amid hopes that the Obama administration will respond favourably.

Direct Brazilian exports to the US dropped to 12.6 million litres in October after spiking in September at a peak of 238 million litres, according to the US Energy Information Administration. Plinio Nastari, director of the Brazilian ethanol consultancy Datagro, predicts that, overall, Brazilian ethanol exports will drop to 3.4 billion litres in 2009 from 5.12 billion litres last year.

The elimination of the duty drawback is seen as the immediate cause of the steep drop-off. The drawback had allowed importers to be reimbursed for the \$0.54 tariff in return for exporting, in most cases, jet fuel.

Nastari says the end of the drawback is having a big impact, limiting direct exports to the US. However, he believes that internal demand in Brazil can absorb the shortfall in exports.

The extension of the tariff irks Brazilians, who see it as the one true barrier to the US market. "There is a lot of pressure [from Brazil] that some measure of flexibility be adopted regarding this tariff," Nastari says.

Matthew Nicely, an international trade lawyer at US firm Thompson Hine, says: "[The bill] is bad government policy. You're talking about a time when we need to expand access to cleaner fuels and access to fuel that is less dependent on imported oil.

"We're simply trying to help the farmers in our country, but in a way that I believe isn't

“The Farm Bill is bad government policy.... We're simply trying to help the farmers in our country, but in a way I think isn't economically or environmentally viable

MATTHEW NICELY



PUMP ACTION: Filling up with ethanol in São Paulo. Brazilian producers hope domestic demand makes up for a fall in exports to the US

economically or environmentally viable."

The bill also cuts a blending credit to US farmers from \$0.51 to \$0.45 per gallon of pure ethanol blended into gasoline.

Although this appears to favour Brazil, a Thompson Hine report says this is not the case: "Brazil claims that the reduction in the US ethanol-blending credit — without a commensurate reduction in the tariff — will hurt Brazilian producers because it will make the price of imported ethanol less attractive than that of domestically produced corn-based ethanol, because the 45-cent credit will be inadequate to cover the 54-cent tariff.

As such, US blenders are more likely to choose domestic corn-based ethanol over Brazilian sugar cane ethanol."

Brazilians neither expect nor want a complete elimination of the tariff. Paulo Sotero, director of the Brazil Institute at the US Woodrow Wilson Centre for Scholars, says they are after "a gradual opening", not an abrupt elimination of the tariff, which would send prices soaring.

Brazil says it will file a case with the World Trade Organisation (WTO) arguing that the reduction in the blending credit gives the US an unfair advantage. However, Nicely says: "There is no reason to take this to WTO litigation. This is too important an issue for climate change."

Producers take long way round and send exports on a Caribbean cruise

CHRISTIANA SCIAUDONE

A Caribbean loophole provides a way to keep Brazilian ethanol exports afloat despite obstacles erected by the US Farm Bill.

As the US extends a \$0.54-a-gallon tariff on their product, Brazilian ethanol producers' best bet (unless they can negotiate away the tariff) is to ship ethanol tax-free to the US under the Caribbean Basin Initiative. At the moment, 2.3 billion litres of ethanol is permitted into the US through the Caribbean. The amount is capped at 7% of annual US consumption, an amount that has never been reached.

The initiative was designed to help Caribbean countries develop economically and diversify their exports. Nevertheless, nearly all of the ethanol moving from the region to the US comes from Brazil.

The amount of Brazilian ethanol exported through the Caribbean was on the rise even before the Farm Bill. It increased to 1.28 billion litres last year from 500 million litres in 2006.

Meanwhile, direct exports to the US dipped from 1.7 billion



PREDICTION: Plinio Nastari

litres in 2006 to 1.46 billion litres last year.

Even with extra shipping and re-processing costs, indirect exports should increase, while direct imports are expected to fall, says Plinio Nastari, director of the Brazilian ethanol consultancy Datagro. Direct exports will probably occur only during peak times when US prices are favourable and Brazilian supplies are high.

Despite the importance of the Caribbean, significant

Brazilian investment in the region is unlikely. Rather, Brazil is focused on clearly defining trade with the US in the form of a lower tariff, not by capitalising on uncertain windows of opportunity.

However, Bob Starkey, vice-president of fuels for Jim Jordan and Associates, a US ethanol consultancy, says the US is unlikely to eliminate the tariff, and if it is reduced, it will not go below \$0.45. "I don't see us abandoning the Caribbean basin to allow Brazil to import cheaper ethanol into the US," he says. "We have a history of support to the Caribbean."

But demand for ethanol in the US is weakening with falling oil prices. "The big difficulty today is that the price of oil is very low," says Joaquim Tavares de Paiva Muniz, an arbitration lawyer who works in the energy sector for the Brazilian firm Trench, Rossi and Watanabe.

Starkey adds: "The only thing keeping ethanol afloat is the mandate that it has to be blended into the fuel supply, otherwise it's twice as expensive as oil. That kind of thing is going to keep Brazilian ethanol out."