CORRECTED VERSION

ENVIRONMENT AND NATURAL RESOURCES COMMITTEE

Inquiry into the production and/or use of biofuels in Victoria

Melbourne — 11 September 2006

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Mr M. Jones, manager, government relations, CSR Ethanol Ltd.

Mr JONES — Gavin Hughes sends his apologies. Barnaby Joyce called an ethanol meeting in Canberra at short notice, so we have split our resources today! I did run the ethanol business for CSR for a while, so I have some background knowledge about ethanol.

The CHAIR — Fine; then I formally welcome you. I advise you, Martin, that all evidence taken by the committee is taken under the provisions of the Parliamentary Committees Act and is protected from judicial review, but if you make comments outside the precincts of the hearing, they are not covered by parliamentary privilege. Hansard will record all evidence given today, and you will be provided with a proof version of the transcript within a couple of weeks. We have 40 minutes set aside for your presentation, so if you would like to perhaps give us your presentation, and leave us about 20 minutes for questions.

Mr JONES — I thought I would just make some fairly brief introductory remarks and leave a bit more time for questions. CSR has been manufacturing ethanol in Australia since 1901. The kind of ethanol we made then was a different sort of fuel. We kept making that until 1986, but we are out of the rum business these days, although a number of people have asked us to go back into it! That was originally in Sydney. Today we operate facilities in Sarina, which is near Mackay in Queensland. We have what we call a polishing unit here in Yarraville, in Melbourne. We have not fermented there for a number of years; it would not be environmentally acceptable to do that at that facility anymore.

So we produce hydrous alcohol at our Sarina facility, and until July we were either exporting our surplus, which is about 50 per cent of our production, or we were moving product down to Melbourne for polishing. At our polishing unit we manufacture grades — we actually have about 100 grades of ethanol. That is quite surprising; we add little bits and pieces according to the different markets we serve. Our primary markets are pharmaceutical, food, paints and inks; and more recently we have been supplying quantities into the fuel market.

The fuel market almost died completely about three years ago with all the scares coming out of the Sydney press in relation to what it may or may not do to motor vehicle engines. I think we were down to supplying about one tanker load per month. We almost sold nothing at the bottom of that cycle. This was all produced in Yarraville.

As things have happened the ethanol market has kicked, largely driven by the independents. The independents were not able to get access to 98 RON, and they saw this as an opportunity to compete in that end of the market, and others saw a marketing opportunity to compete with the shopper docket schemes.

So while the major oil companies were still doing trials and gradually moving their way into the market, the independents really gave it a kick-start. While we had a $15 million construction project under way in Queensland to make fuel ethanol, and we thought we would not invest anything in Yarraville, in fact the market kicked so hard that we actually expanded the Yarraville plant as well. In July this year we brought on our fuel ethanol expansion in Queensland, and between Queensland and Victoria we now have 50 million litres of fuel ethanol capacity.

In relation to the other markets I mentioned — pharmaceuticals, food and so on — those markets are really not growing. They are growing at less than half a per cent a year, so in fact in terms of the economy they have a decreasing share; they are not growing with the growth in the economy.

I forgot to mention that we make the best vodka in the Asia-Pacific region down here, and we generate exports for Victoria into Asia, which is something we want to keep going. But the big opportunity really for the ethanol industry is in fuel. It is potentially a large market. Depending, of course, on where substrate prices go and where oil prices go, it could be quite an attractive market.

To that end, last Monday we announced that we are looking at supplying northern markets and southern markets, and that would entail major investment in one or two plants. That could be in Queensland; it could be in New South Wales; it could be in Victoria; it could be two of the three states. That will be driven to a large extent by the relationships and the demands that we have from our customers and the ability to find suitable locations.

We believe — and our studies are showing — that to be successful in this business, you need to be world scale. When I first started we thought world scale was 80 million litres — that was about three or four years ago — and we were looking at expansions based on molasses of that order. We would say today that you need to be at least 200 million litres. The largest US plants are now pushing up around 400 million litres a year.

We have done a lot of work on substrates. Typically ethanol is made in Brazil, for instance, from sugar. In Australia CSR has made it from molasses, and in the USA the predominant substrate is corn. It is our view that the only substrate that is economically attractive in Australia today is grain, and we would expect that our new investments will be based on grain. The preferred grain is sorghum. It is primarily used in the feed market for cattle, but it is the easiest to process and has the best returns. In Victoria I do not think there is any sorghum to speak of, so any facility down here would be based on wheat.

The models that we are looking at are grain based. It is hard to say how far this industry can go. If you look at a 200 million litre plant, that needs about 475 000 tonnes of grain, so when you consider the types of grain that might be available, obviously you have to look at the value chains that are out there today and you are buying it out of those value chains. You need to look at where the nodes are in terms of where grain is delivered. It is important if you are going to get a positive life cycle outcome from a greenhouse point of view that you have access to gas. In 1944 CSR built a distillery in Warracknabeal. The location had some political interference at the time. The investment was made. It ran for six weeks because 1944 was a drought year and there was no water to run the distillery and there was no grain to put through it, so we have deep memories of a failed investment which was really part of the war effort. Water is important, it is important to have gas, and you need to be in a region where grain naturally flows towards your installation. Of course you need proximity to your customer market.

Fuel is all about logistics and minimising supply chain costs, so we are quite optimistic about the future for ethanol in a somewhat limited way. I think if Australia achieved 10 per cent in its fuel blend — I do not mean E10 as a regulated fuel, but if we got 2 billion litres of ethanol in the market, I think that would be quite a substantial achievement for Australia with today's technologies. That probably concludes my remarks and I will pass it back to you, Chair, for questions.

Mr DRUM — If we are to get 2 billion litres into the market, where is it likely to come from?

Mr JONES — I think all the future investments in Australia are going to be grain based unless there is a technological breakthrough.

Mr DRUM — How do we grow so much more grain?

Mr JONES — I do not think Australia has the prospects of growing a lot more grain. I think if a grain-based ethanol industry gets off the ground, you will start to find that farmers will look for grains that have higher starch content that can improve the yields. We can look at the sorghum that is grown, and we have had four lots of sorghum go to the US for pilot plant runs and so on, but there are higher starch content grains, and you may get farmers, if they are under contract and so on, to shift towards those, and people may well start trying to breed crops that way.

Mr DRUM — Is there a potential market for what we used to call seconds? Is there a potential market for seconds for fuel, whereas food still becomes the primary source of A-grade grains?

Mr JONES — Yes.

Mr DRUM — Is there a potential in this area?

Mr JONES — Yes, a good potential because distilleries are not that fussed; they are looking for the starch content, so it is damaged grain and lower grade grains. Trying to buy it out of the pasta segment, for instance, which is a specialised high value add, is not going to happen. Australia produces about 20 million tonnes of grain a year and about 17 million tonnes are exported, so I do not see Australia itself is going to particularly go short.

Mr HILTON — It is my understanding — and correct me if I am wrong — that to produce a litre of ethanol takes about 2 litres of water.

Mr JONES — It is actually simply cooling water. We are on total recycle, except for cooling.

Mr HILTON — So if we are in a period of drought and climate change, do we have the water resources which are going to be required to produce the ethanol, and is that the most efficient way of using what is a diminishing resource?

Mr JONES — We will not be building in locations where we do not have a surety of water. I explained the experience we had in Warracknabeal with the drought, so we need to be in locations where water is available.

Mr HILTON — Presumably then you are using water which cannot be used by other people?

Mr JONES — There is a price on water. There are recycle opportunities. In relation to our distillery in Queensland, the water that is produced out of that process gets recycled back, but the demand is primarily for cooling, so if you can segregate steam where you may need a higher quality from perhaps a lower quality, and there may be opportunities working with regional areas perhaps to reuse grey water, we would be looking at those sorts of things.

Mr SEITZ — In 2011 there is the potential downgrading of subsidies for ethanol under the grants production. How do you see that affecting you because it will make it more viable to import ethanol?

Mr JONES — On 1 July 2011 the market goes open. There is no protection against imports, and that is what is driving us to world scale.

Mr SEITZ — So you will be able to compete against imports?

Mr JONES — If we cannot compete against imports, we will not be investing $200 million in a distillery. Even the investment we just completed in Sarina, even though it is 2006, we have assessed that against imports.

Mr SEITZ — What are your thoughts on mandating the amount of ethanol in fuel mixture?

Mr JONES — We think that a more robust market will develop if it is allowed to develop of its own accord. There are barriers. Governments have been addressing the removal of those barriers to the market developing. I think that going down the path of a mandate now will get everyone distracted. We believe the market is poised for growth; we do not see market failure.

Mrs COOTE — You spoke about expansion and you spoke about expanding into Queensland, New South Wales and Victoria. Do you think that Victoria, at Yarraville, has the potential to meet the growth in demand that you have foreshadowed?

Mr JONES — No, Yarraville does not — not at all — and that is not the right place to build a distillery that is bringing in 400 000 tonnes of grain. It is not bad from an ethanol point of view because we are quite close to the terminals down there, but if Victoria is one of the locations we choose, it is more likely to be regional.

Mrs COOTE — So just because Yarraville is not going to be a potential site, it does not rule out Victoria against New South Wales and Queensland?

Mr JONES — No. We need about 10 hectares and we do not have 10 hectares at Yarraville. You would not really build a distillery in a built-up residential area.

Mrs COOTE — You spoke about water and you spoke about the grain, obviously, and also the transport issue of getting it to a refinery. Therefore, how far within Victoria from Melbourne in distance would you see to be viable, because obviously Warracknabeal was not?

Mr JONES — No. You need gas. We have not picked a location in Victoria yet. I have meetings with State and Regional Development later in the week, but we would be looking from, say, Geelong to central Victoria, through that corridor.

Ms DUNCAN — Can you expand a bit on those barriers you were referring to earlier?

Mr JONES — Yes. It has been interesting to see how the market has evolved, and maybe the oil companies have more information than we have on this. I believe something like 50 per cent of motorists still will not try ethanol, but the numbers are changing in Queensland, and the Queensland government has been a very strong supporter of ethanol, and has been building the E-brand. They had Jack Brabham as an advocate. They used it in their own fleet. They have a huge fleet there.

They have just generally promoted it. They are talking about a mandate, too; I do not know whether that will happen. So with Queensland motorists we are starting to see a shift — it is becoming more and more readily available in Queensland, so people are trying it. In fact I think a number of outlets do not carry ULP any more. With our customers we have seen a new site in Sydney, for instance, that went to levels of E10 straight off and they considered whether they would continue to run ULP with it because the demand for E10 was so strong. Some of these are at discounts and some are not.

Ms LOVELL — You talked about the future of ethanol production being grain based. If ethanol production in Australia was to expand in the future, would Victoria have a climate suited to the production of ethanol feed stocks or would we find ourselves at a disadvantage to other states due to growing conditions et cetera?

Mr JONES — Yes, there is a slight disadvantage here because in our view sorghum is the preferred feed. Wheat tends to foam in facilities and it makes it a bit harder to operate, but it would not rule it out. You can have plants that will run both, but in Victoria I think it is more likely to be wheat based. I would not rule it out. It is a slight disadvantage but with these things you are always weighing up a whole lot of factors and to a large extent we will be driven by our customers.

Ms LOVELL — So what climate is best for sorghum?

Mr JONES — Darling Downs, northern New South Wales.

Mrs COOTE — Get rid of the cotton.

Mr JONES — Yes. Well, that is another thing. I think someone talked about switching crops, and it may be that cotton farmers switch out of cotton.

The CHAIR — Are there any specific logistical problems that work against Victoria?

Mr JONES — No, none that is a show stopper for us at this stage.

The CHAIR — Could I have your opinion of whether introducing ethanol into petrol is the best way to reduce the environmental impact of our fleet?

Mr JONES — I do not know whether it is the best way. Ethanol is a renewable fuel, we can make it here, and it does have some environmental benefits. Whether there are other ways to achieve the same environmental outcomes, I do not know.

Mr DRUM — In light of the presentation before yours, in relation to the shortage of grain here in Victoria and the fact that it is all being used at the minute, what do you see happening? Should we introduce and encourage a vibrant ethanol industry and market in Victoria? Do you see that industry pushing the price of grain up above the stockfeed market?

Mr JONES — I have not seen the grain balances for Victoria. Gavin has had a study done nationally around Australia. We have looked at each location where grain is being handled, where it comes in to nodes. We have looked at the drought factors, and the drought factor as it impacts the ethanol business relates to the size of the plant. So you might be able to build 75 million litres in a lot of locations and not have a drought impact; but if you wanted to build 200 million litres in those locations, you would have a drought impact. We are looking for locations where there is not a drought impact.

The other thing is that if it is possible to get locations within 40 kilometres, I think it is, of ports, we can import grain. One thing about an ethanol industry is that if you have contracts with oil companies, they will expect you to keep supplying, no matter what, so that is an important factor for us — and the motorists keep expecting to have it shown at the pumps, surprisingly enough.

Mr DRUM — If we were to get E10 in Australia and everybody was to use it, how many billion litres would we need per annum?

Mr JONES — Two billion.

Mr DRUM — How much grain would we need to produce 2 billion litres?

Mr JONES — Four to 5 million tonnes, something like that.

Mr DRUM — And you are saying we have a 20 million tonne harvest?

Mr JONES — Yes — a 17 million tonne surplus.

Mr DRUM — So we produce 20 million tonnes and we would need to commit 4 or 5 million tonnes of that — —

Mr JONES — Of the 17 million.

Ms DUNCAN — Is there anywhere in Australia that does not have water issues?

Mr JONES — It is all a matter of degree.

The CHAIR — Thank you very much, Martin, for your time.

Witness withdrew.