

Oil Market Report: April 2018

Such has been the fuel price volatility experienced in April, that the mandated rise in UK fuel prices – as a result of increased biofuel content – was largely missed by commentators and consumers alike. As of April 15th, it became the law in the UK for all road fuels to contain 7% bio content (an increase from 4.75%) and with biofuels (methyl esters for diesel and ethanols for petrol) trading at higher prices than neat fossil fuels, increasing the bio content put up prices by around 0.50ppl. Based on current annual consumption of petrol and diesel (50bn litres pa), that's an increase in cost across the UK of circa £250m.

But as April demonstrated, in a market where prices frequently go up and down by 0.50ppl on a daily basis, the effect of this change was muted. Which may be no bad thing for the future, because UK consumers can look forward to further increases next year, when the mandated minimum level of biofuels in petrol and diesel will increase to 8.5%. Thereafter the percentage increases will be smaller, but will nonetheless be on an annual basis, so that by 2030 the agreed target of 12% biofuel content (about 6bn litres per annum) will have been met.

6bn litres is not a small volume by any standards and depending on the provenance of the product (more of that later), it will play a significant part in the decarbonisation of the UK transport pool. The figure is also all the more impressive, when one considers just how young the Biofuels Industry actually is. It was only in the 2004 Energy Act that the UK began to formulate laws that allowed changes to road fuel specifications (ie, the addition of biofuel) to help tackle climate change. Even with that legislation in place, it was still another 4 years before a mandated minimum biofuel content became law (this was the first year of the Renewable Transport Fuels Obligation = RTFO).

Early biofuels policies in the UK (and around the world) had good intent, but were often ill-thought out in terms of consequences. For the main part, the initial targets were way too ambitious and because this forced the pace of change before the industry was able to comply, numerous ethical and environmental own goals were scored. In their rush to hit required targets, the UK and other EU countries provided an indirect incentive to increase palm oil production (this to make Palm Oil Methyl Ester = POME = a type of biodiesel). This in turn led to the rapid deforestation of parts of South America and South-East Asia, to make way for palm oil plantations. Differing tax treatments across different EU countries also created duplicated supply chains. For example, the zero duty treatment of biofuel in Germany (ie, no tax) meant that producers from other countries sent their product to Germany rather than consuming it locally. This not only meant unnecessary extra transport emissions, but outside of Germany, it increased the reliance on non-EU biofuels – often of doubtful origin. Finally, in the USA, subsidies for mid-western farmers meant that ethanol for petrol typically came from corn. Scientists were quick to point out that this was a process that usually required more energy, than simply extracting crude oil and refining it in the normal way.

However, the industry has moved on a great deal in 10 years and new legislation is further ensuring that the mistakes of the past are not repeated. A “crop-cap” will be introduced in 2018, aimed at addressing “fuel for food” concerns and this will limit the amount of crop-derived biofuel (eg, Wheat, Soya, Sugar) to 55% of total production. The rest will have to be made up of waste biofuels (eg, Tallow, Used Cooking Oil) and this percentage cap will be reduced each year so that by 2030, only 20% of biofuels will be permitted to come from crops. Furthermore, most of the industry has self-policed its activities in recent times, thus improving the reputation of the biofuels supply chain. The result was that in 2017, precisely zero litres of palm oil went into the production of biofuels in the UK, compared to over 10% back in 2010. In the same period, Used Cooking Oil (arguably the most environmentally friendly product, because of its local sourcing – we do like a chip butty or two in Britain – and its relative ease of processing) has increased from 5% to 40%.

Despite this progress, the general public remains somewhere between ambivalent and sceptical when it comes to the biofuels industry. Some remain outright hostile, which is a shame because not only does the introduction of sustainable biofuels help decarbonise transport (every litre of Used Cooking Oil delivers a 70% reduction in Greenhouse Gases versus standard diesel and bio from tallow can achieve up to 90%), but all progress has been achieved with minimal subsidy from the Government. And this surely is a good thing in a world where tax payer money is splurged on renewable energy projects that are for example, still stuck on the rights of breeding newts, or on power stations in the North of England, that receive hundreds of millions of subsidised pounds to import wood from the USA and generate electricity of marginal environmental benefit.

The biofuels industry (which is largely run by the oil industry) by contrast, stands out as a sector that has put its own money where its mouth is. This despite the fact that the sector has been forced to reduce sales of its core product (ie, petrol and diesel from crude oil) by 5% and been asked to replace it with something considerably more expensive! As a result, 6bn litres of crude oil has been removed from UK consumption and if you multiply that by all the

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countries around the world doing the same thing - you have a credible and material reduction in CO2 emissions.

