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Q and A: How Will Changes to U.S. Ethanol Subsidies Affect Brazil?

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Last month, U.S. senators introduced competing legislation regarding the ethanol producer subsidy and import tariff, which are set to expire this year. A bill proposed by Democrat Dianne Feinstein (Calif.) and Republican Tom Coburn (Okla.) would eliminate the 45-cent subsidy for ethanol producers and 54-cent tariff for ethanol imports, while legislation from R Senators Charles Grassley (R-Iowa) and Kent Conrad (D-N.D.) would sharply reduce, but still retain, the measures. What are the advantages and drawbacks of the bills and is one likely to pass? How would the legislation affect the ethanol industry? Does Brazil have the infrastructure and capacity to take advantage of new ethanol export opportunities abroad?

A: Jim Kleinschmit, director of the Institute for Agriculture and Trade Policy's Rural Communities program:

"The Volumetric Ethanol Excise Tax Credit (VEETC) is not about whether the United States will use biofuels (that is covered in the Renewable Fuel Standard II), but only how much, at what cost to U.S. taxpayers and, based on the associated import tariff, from where they will come. The competing Feinstein-Coburn and Grassley- Conrad proposals to alter VEETC show that even ethanol's staunchest supporters recognize that biofuels policy needs to change, but the economic impact of either proposal—beyond taxpayer savings—is not obvious. Elimination or lowering of the blender credit is expected to result in at most relatively small decreases in overall ethanol production and use. The additional infrastructure support should help increase biofuel availability, but the real limit in expanding biofuel consumption in the United States is the current 10 percent blending wall, which the EPA is currently considering raising. Elimination of the tariff could have more severe consequences. Expectations of market access could accelerate large-scale investment in biofuels development internationally, which can have serious human rights and food security implications for local communities. But whether the capacity will actually be there to export is not clear: higher sugar prices and reduced production due to weather caused Brazil to import significant volumes of ethanol in 2010-11. Such annually disrupting factors, especially as the climate changes and global food and energy demand increases, illustrate the real dangers associated with making biofuels, which can provide so many economic and sustainability benefits on a local level, into a globally traded commodity and depended-upon energy source."

A: Bruce A. Babcock, professor of economics at Iowa State University:

"These two proposals reflect the new political reality in Washington that portends an end to the price subsidy, thereby eliminating and remaining justification for the ethanol import tariff. Given the huge efforts to keep both in place, one would expect their elimination would mean financial ruin for U.S. ethanol and boom times for Brazil. But high energy prices will keep demand for ethanol strong in both countries. And growing U.S. mandates will underpin demand so much that the United States faces ethanol shortages in just a few years. Changes to U.S. policy will have little impact on Brazil because strong domestic growth in flex-fuel vehicles combined with a lack of investment in new plants and sugar cane fields means that Brazil cannot even meet its own needs for ethanol. Brazil needs to ramp up production by more than 30 percent before it will have significant amounts of ethanol to export. And even if Brazil achieves such impressive growth, what it exports to the United States will be imported as a low-carbon ethanol source to help meet California's low-carbon fuel standard or as an advanced biofuel under the U.S. Renewable Fuels Standard. The U.S. ethanol industry would be best served by following Brazil's example and expanding the ability of the U.S. vehicle fleet to use ethanol rather than using its political clout to maintain subsidies and protection from competition. Elimination of trade barriers and subsidies would make a bright future for ethanol in both countries even brighter."

A: Marie Brill, senior policy analyst at ActionAid USA:

"U.S. corn ethanol benefits from a mandate for production, blending targets, subsidies and a tariff. This incentive cocktail has fueled industry growth, putting strain on U.S. stocks resulting in price spikes and contributing to current food price volatility. The Coburn-Feinstein bill would cut the subsidy and tariff at the same time. It would have little impact on demand or production, since the mandate would remain, but it could help drop prices by as much as 7 percent. The Grassley- Conrad bill would only lower the current subsidy while crude oil prices are high, but it would increase resources for ethanol infrastructure. While the Coburn/Feinstein bill would help bring U.S. food and energy policies into better balance, the Grassley bill would further invest the United States in corn ethanol as a dominant biofuel. For many years, Brazil has been trying to gain more access to the U.S. market for sugar ethanol. The level of investment in Brazil's ethanol production chain has grown significantly. BNDES (National Bank for social and economic development) investment grew from $445 million in 2003 to $3.8 billion in 2010. Production has more than doubled in the last 20 years to 8 million hectares, and could grow to 4.3 million by 2020. From a right to food perspective, the opening of new markets for ethanol will not benefit the poorer and more vulnerable people. Brazilian sugar ethanol production is based on large-scale monocultures with significant agrochemical inputs that have many social and environmental impacts, including land and income concentration."

The Energy Advisor *welcomes responses to the Q&A above. Readers can write editor Gene Kuleta at* kuleta@thedialogue.org *with comments.*