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Bio-Fuels

Indonesian Biofuel Set to Take Off?

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Report Highlights:

On January 9, 2007, 67 agreements for biofuel development were signed in Jakarta during an event hosted by the Ministry of Energy and Mineral Resources. Government policy will likely be the most important factor in determining whether the burgeoning biofuel industry in Indonesia will be a success.

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Indonesia Seeing Heightened Interest in Biofuel

On January 9, 2007, 67 agreements for biofuel development were signed in Jakarta during an event titled the Joint Initiative for Biofuel Development. The estimated investment value of the contracts is \$12.4 billion. Another \$2.8 billion will be financed by the national banks Bank Mandiri and BNI. The Indonesian government's bank interest subsidy program will support the financing. The Ministry of Energy and Mineral Resources hosted the event, which was attended by 7 governors and 18 county officials.

The agreements were signed by 52 foreign, local, and state-owned enterprises that are either planning to invest or have interest in investing in biofuel development in Indonesia. There were 12 financial institutions and 11 foreign-Indonesian joint ventures. Over a third were indicating interest in biofuel industry investment. Three ventures account for over half of the value of the agreements: CNOOC, the China National Offshore Oil Corporation, will invest \$5.5 billion in PT. Sinar Mas Agro Resources and Technology Tbk and Hong Kong Energy; Genting Biofuel Asia Pte. Ltd. will invest \$3 billion in PT. Pembangkit Jawa Bali and have the support of the government of Kabupaten Merauke to develop crude palm oil (CPO), sugarcane, and jatropha plantations and biofuel production plants; and Indomal Group, a joint Indonesia-Malaysia venture, will invest \$1 billion to develop a CPO plantation and biodiesel production plant and have the support of the government of Kabupaten Sula Islands on North Maluku. Among the agreements, 7 are for research and development activities and 12 will involve local governments in their approach.

Plans for the development of an Indonesian biofuel industry would be concentrated in the eastern part of Indonesia, due to the availability of land where raw materials can be produced. Most efforts are focused on Kalimantan and Papua, with others on Sulawesi and Maluku Islands. Currently, CPO production is focused in Sumatera in western Indonesia and Kalimantan.

Potential Hurdles

The recent announcements reflect the current enthusiasm for a biofuel industry in Indonesia, though short-term increases in production will be limited to a few firms. There are currently only two companies who sell biodiesel from CPO to Pertamina for mixing with local diesel, while a few other are producing biodiesel on a small-scale for their own use. Another two firms are producing ethanol. FAS/Jakarta is aware of eleven firms that are in the process of constructing new plants or expanding existing ones. If these firms were to reach their targets by the end of 2007, almost 2.5 million tons of biofuel, mostly biodiesel from CPO, would be produced in Indonesia during 2008. This would represent a large increase over current production, which is around 300,000 tons.

Despite the enthusiasm, there are several areas of concern. The price of CPO, which is already affected by the tight supply of edible oil, is increasing further in response to the potential demand for biodiesel. Large increases in demand for CPO for biodiesel will compete with CPO for edible oil over the next five years before new plantations can produce additional CPO. If the price of petroleum remains relatively

stable and the rush of building biodiesel plants occurs as announced, the CPO prices will be so high that the price of biodiesel will not be able to compete with petroleum. Unless petroleum prices are also high, biodiesel production will be dependent on government subsidies.

Jatropha is also being considered by the Indonesian government for biodiesel production. It has a relatively high yield per hectare and can be grown on marginal and degraded land. However, it could take years to determine the variety of Jatropha that is best suited to the various types of soil throughout Indonesia, the right planting method, the right post harvest handling, and the right technology to produce biodiesel from Jatropha.

Another concern is the by-product of biodiesel production, glycerin. It accounts for approximately 10-12 percent of the weight of biodiesel produced. An additional 250,000 tons of glycerin will likely create an oversupply on the world market and depress prices, decreasing profits for biodiesel producers.

The heightened interest in switching from petroleum to biofuel is the reaction of the unstable world petroleum price and government policy. This is evidenced by the fact that some of the firms who signed contracts are new to the agribusiness sector. Given the above, a biofuel industry in Indonesia faces many hurdles for the short term. Government policy will likely be the most important factor in determining whether the burgeoning industry will be a success.

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