



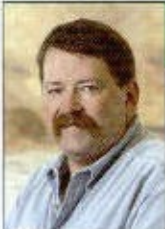
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A MONTHLY NEWSLETTER OF THE LATEST PELLET FUELS INDUSTRY NEWS

PFI President's Message



Changes. I was speaking to another pellet producer this summer, discussing the current supply situation on the East Coast. He related to me that no one was returning his sales calls in April, but his phone was ringing off the hook in May. Another producer in the mid-West was (and still is) sitting on thousands of tons of fuel left over from last winter. Another producer, who makes pellets for non-residential heating, said in June that he hadn't made any residential product "in months". For the last two Januarys (that's the dead of winter folks) my company was sitting on huge amounts of fuel, yet we were "sold out" earlier in the season. I just finished reading retailer comments in the August issue and the fuel industry was blasted for the shortages that are now being experienced on the East Coast. If you read my columns before, you know I harp-preach-whine-grumble about planning between manufacturers and retailers. It goes both ways.

There is fuel out there, but unfortunately it is in the wrong location so logistical costs come into play. As we have seen in the past, some of this shortage is panic driven which means later in the season, fuel will free up. A lot of capital has been spent in our industry trying to satisfy these spikes in demand. Companies have risked their financial futures investing in high freight cost fuel or have built plants in locations that had no logical premise for development other than a spike in demand. Inventory financing costs are huge, and can kill a company. Look what happened when a certain well-known stove company built capacity and a HUGE inventory, and the market died. Luckily the current spike started much earlier in the year than the Katrina spike.

The current price of oil has changed the dynamics of our marketplace. Obviously it spiked demand in stove and fuel sales. But fuel producers get a double whammy with diesel fuel surcharges on both incoming raw material purchases and outgoing shipments. The housing crunch has also hit our producers hard as the amount of raw materials available has dropped. Add to that whenever fossil fuel prices increase industrial and commercial users that can burn wood residue's jump into the market, further reducing supply. Raw materials costs have more than doubled for many producers in the last three years. At our annual meeting in Hilton Head last month, an overwhelming number of North American pellet fuel producers indicated they were having significant raw material "challenges" this year. *This is why our industry has to move away from premium grade fuel, and into higher ash pellets made from raw materials that are exponentially more plentiful, and generally less expensive.*

The market for wood pellet fuel is growing all over Europe. The amount of fuel used there dwarfs the North American market. Austria, with its population of nine million, consumes

about half of what all of North America's 350 million people consume. Italy sold over 350,000 pellet stoves as compared to our 54,000 units last year. It's embarrassing. Most of the new capacity built in North America, as measured by installed horsepower, is located outside of our traditional heating markets and is headed to Europe. Why? Because the millions of dollars necessary to build these plants is premised on firm contracts to sell product, no matter what the weather or current market conditions are. As the North American market grows from space to central heating and bulk distribution, more capacity will be built which should be able to handle these spikes. I predict that fossil fuel prices will continue to be in the \$100/bbl range, and in the five to 10 year time frame the fuel required for space heating will be only 10-15 percent of the total North American pellet fuel market.

The PFI held its annual meeting and conference at Hilton Head on July 20th with a record attendance of 300 people. I am very happy to report that PFI membership approved the major change to our fuel standards that took five years to complete. Besides adding Super Premium and Utility grades, there were some variations and additions of fuel parameters. The biggest addition was the approval of an industry wide quality control and assurance program. This includes compliance testing, product registration and new product labeling. There is more information on our Web site www.pelletheat.org. It will take two years to fully implement.

And after four years of being the PFI's president, the reins have been handed over to Scott Jacobs from Ozark Hardwood Products, Jeff Thiessen from Dansons Group is the new Vice President, and Bob Sourek from Bear Mountain is Secretary-Treasurer. Scott has been a very active director and committee member and has chaired our conference committee. Troy Jamieson from Somerset Pellet Fuel and Chris Sharron from West Oregon Wood Products were elected to our Board. I would like to thank TJ Morice, Ron Leofsky and Rob Davis who served with me on the Executive Committee for the last four years. I will be chairing the Government Affairs Committee, trying to get pellet fuel on parity with other alternative energies. And if Congress does its job before they recess for the election, we might see some tax credits for pellet appliances. Stay tuned!

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