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AUSTRALIAN RENEWABLE FUELS LIMITED

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Australian Renewable Fuels (ARW) operates two biodiesel plants in Australia. The supply, quality and price of feedstock for biodiesel production have been issues for the Australian biodiesel industry. You had operational problems with feedstock in the December 2006 half year. How have you addressed the quality and cost issues? What are the details of your feedstock supply arrangements?

CEO Australia John Lillywhite
After a sharp learning curve we now have a good understanding of all the feedstock issues that arose from the variability of quality and characteristics between each delivery. Over the last twelve months we've developed operating procedures to ensure quality continuity, including tightening our feedstock specifications, improving quality control, plus off-site pre-processing filtration. We've developed our own in-house feedstock filtering system for implementation in the capital works program, which will reduce our feedstock costs and improve the associated logistics.

Minimum savings of $0.02 per litre of finished biodiesel are expected. We'll also trial the processing of cheaper grade tallow feedstocks through these filters with a reasonable expectation of savings in the order of $0.04 per litre.

Despite the early problems, we've established a strong reputation for delivering top quality biodiesel that meets all industry standards. We've invested in a biodiesel certification laboratory at Largs Bay and a process control laboratory in Picton to ensure we maintain our reputation for high quality biodiesel.

Feedstock typically accounts for 60 to 70 percent of total biodiesel production costs. Our feedstock cost management strategy is to maximise our margins by using the highest possible proportion of tallow which is currently the cheapest high volume feedstock available in Australia. Our blends will be made up of a high portion of hard fats (tallow) and soft oils, such as canola or soy. Using significant proportions of soft oils is not viable at current prices. For example, due to the drought, canola prices have risen by more than 60 percent since early 2006 and at over $1,200 per tonne are now double tallow prices.

We have a five year arrangement with Gardner Smith to provide feedstock up to the plant design capacity on a cost-plus basis. We're working with them to build a strong mutually beneficial and profitable long term relationship. We also have the flexibility to take some feedstock from other suppliers.

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You've achieved the production volume and quality necessary to qualify for the remaining $5.4 million of the $7.2 million Commonwealth Government's Biofuels Capital Infrastructure Grant. What are the implications for your business?

CEO Australia John Lillywhite
The Grant is a very significant milestone for Australian Renewable Fuels. Our achievement of independent expert certification of the consistent quality and volume benchmarks required to achieve the Grant is the best verification for our customers and the market generally of our ability to reliably produce commercial volumes of quality biodiesel. It will give customers the certainty they need that we are a dependable supplier.

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You moved from developer to producer with the Largs Bay plant, near Adelaide, opening in March 2006 and the Picton plant in Western Australia opening in July 2006. What are your production offtake arrangements for both plants?

CEO Australia John Lillywhite
We've already achieved significant sales for both Adelaide and Picton with a range of customers from the international oil majors through to local distributors and retailers. To date we have delivered 8 million litres from the Adelaide plant under the supply contracts that we commenced last October. We've also maintained discussions with the European trading house, Godiver, for delivery of biodiesel into the contract that was written in 2004.

Our February production and sales of biodiesel were:

million litres	Production	Sales
Adelaide	2.4	2.0
Picton	1.2	0.2

Production and sales for March and some of the June quarter will be impacted by implementation of the capital work program.

Our target is to have the Adelaide plant's entire 45 million litre production and 70 percent of Picton's 45 million litre capacity committed by the end of calendar 2007. That is the equivalent of 76.5 million litres with a current market value of approximately $80 million on an annual basis. We believe that's achievable.

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The biodiesel industry in Australia is very immature. What are the drivers that will lead to the acceptance of the fuel as an alternative to mineral diesel? What are your target markets?

CEO Australia John Lillywhite
Biodiesel is a clean-burning diesel fuel produced from renewable resources and compared with petroleum diesel it has significantly lower exhaust emissions of a variety of pollutants resulting in significant positive health impacts. The market is now beginning to understand and accept biodiesel as a modern fuel with much less impact on the environment than traditional mineral diesel. Demand for action on the environment, greenhouse gases and climate change is rapidly gaining momentum at the community, business and political level. Now is an opportune time for the industry and for us to demonstrate the significant benefits of biodiesel for the community and government.

Large diesel users, such as earth moving and resource companies, are becoming increasingly sensitive to environmental issues and are asking their mineral diesel supplier for a blend of biodiesel in their fuel, in a range of 5 to 20 percent, to reap the benefits of lower exhaust emissions at no increase in fuel costs. Our aim is to provide that blend to the local distributors and oil majors servicing those customers.

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You are using the Energea process. How does it compare with other biodiesel technologies in use in Australia?

CEO Australia John Lillywhite
The Energea process we use is specifically designed for the continual processing of tallow or used cooking oil, as well as vegetable oils, as feedstock stream. It's cheaper to operate than the old batch process technology some others are using.

Feedstock flexibility is a key competitive advantage. Some other technologies are restricted to processing liquid vegetable oil which is currently so expensive it is not a viable feedstock. It is a continuous high yielding process with minimum environmental emissions. Another significant advantage of this technology is the acceleration of the transformation process. The streamlined continuous process produces high-quality standardised biodiesel from raw materials which are local and renewable, using less energy with less capital investment.

To date, its adoption has been constrained by the relatively small size of Energea. Because of Energea's limited resources we had to employ and develop our own technical personnel to fine tune the plants, which is one of the reasons for the delay in production. In the last 18 months we have become self sufficient in the technology and are now the international experts. Based on our successful optimisation of the processes, we expect the Energea technology to spread to other markets.

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The biodiesel industry is heavily subsidised and the use of biodiesel mandated by governments in the US and in Europe because it is a clean, renewable fuel. What other government support is there for the Australian biodiesel industry in addition to the Grant? What is the Government's alternative fuel policy?

CEO Australia John Lillywhite
There is no explicit support other than the once-off capital development grant available to certain biodiesel producers. There is a producers' grant equivalent to the excise payable on biodiesel production, however, that's offset by the July 2006 loss of fuel tax credit for most biodiesel applications. We expect that the Government may be more explicit about an alternative fuel policy during the run up to the 2007 election. There are many things the government can do to promote the use of biodiesel at no cost to the taxpayer.

We are working with the Department of Environment to gain support for some technical changes to the biodiesel standards that would allow us to access different and potentially cheaper feedstocks.

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You have purchased Energea's biodiesel technology patents for North America and established a subsidiary in the US with Energea, ARF Inc., and appointed a CEO and President. What is your strategy for embarking on biodiesel production in the US? How will the planned US plant be financed?

CEO Australia John Lillywhite
Australian Renewable Fuels is seeing significant upside opportunity in the US, where the incentives and subsidies for biodiesel production are much greater than in Australia. For example, there is a Federal blending credit for eligible biofuels of effectively US$1 per gallon. In the US there is a significant volume of tallow and other feedstocks that are viable. Our US subsidiary, ARF Inc., plans to develop its own plant in New Mexico where the government has welcomed us with a range of grants and concessions as an incentive to develop a plant in that State.

Also as the owner of the Energea technology rights in North America, we will sell licences to other companies wishing to use the technology. The US company is a standalone venture: there is no further equity or capital committed by the Australian operation. The US subsidiary will be undertaking its own capital raising program.

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You are currently raising $14.8 million in new equity with a placement and a rights issue. How will you use these funds?

CEO Australia John Lillywhite
The conversion of loans from shareholders into equity via the rights issue will account for $4 million. We'll use $3 million to repay a bank facility which will, however, continue to be available to us should it be needed. The investment in high volume tallow processing and methoxide production infrastructure to reduce feedstock quality risk and lower operating costs will cost some $5.6 million. The balance of the funds will be working capital.

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Your March Prospectus does not include earnings forecasts. When do you anticipate generating positive cash flow? What earnings guidance can you provide?

CEO Australia John Lillywhite
We'll have a better idea of the outlook when we've completed our capital works program towards the end of July and normalised production. We expect to become immediately cash flow positive from operations on resumption of full-scale production.

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Thank you John.

For more information about Australian Renewable Fuels Limited visit www.arfuels.com.au or contact John Lillywhite on 08 9363 3500.

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