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Weekly Outlook: How Bad Will Ethanol Demand Destruction Get?

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Recent ethanol plant closures and production slowdowns open up the possibility of demand destruction in corn used for ethanol beyond current projections. Some of the latest predictions saw very dire consequences with upwards of one billion gallons of lost ethanol production in 2020. The worst-case scenarios, like most dismal predictions for the economy, depend on the depth and length of the economic slowdown. An expectation of additional losses in corn use this marketing year from reduced ethanol production seems unavoidable.

Last week's extraordinary negative oil price event brought into focus the enormity of the demand destruction impacting the oil complex. Gasoline stocks continue their climb to record levels. At this point, extensive closures of refineries look necessary to slow the buildup of gasoline inventories. Initial attempts to reboot the economy may show some demand improvement, but many areas jump-starting their economies remain in relatively low population areas. Gasoline demand saw a slight increase as of April 17, after dropping almost 43 percent between March 28 and April 3. At 5.311 million barrels per day, the 4.5 percent increase over the previous week may signal a bottom for gasoline demand. The path back to normal gasoline demand levels looks long and arduous. Ethanol production looks to follow gasoline's lead.

Weekly ethanol production fell for the eighth consecutive week according to the EIA ethanol production report for April 17. Since March 13, ethanol production dropped by almost 46 percent. Current estimates place total idled or reduced production capacity at or above fifty percent of normal. Production fell to an extremely low of 563,000 barrels a day last week. Meanwhile, despite lower production, inventories rose to a record-high 27.7 million barrels. An expectation of continued lower production looks to be in place over the next couple of weeks as more plants lower production or go offline.

USDA dropped corn use for ethanol in the April WASDE report by 375 million bushels for this marketing year, down to 5.05 billion bushels. Further reductions look probable. If the corn conversion rate seen in February extended through March and into April, corn used for ethanol through April 17 sits near 3.25 billion bushels. In projecting corn use for the rest of the marketing year, production assumptions must be made based on the likely pace of economic recovery. It seems doubtful that ethanol plants will be able to ramp up production quickly, even under a rapid recovery scenario. While gasoline demand may provide a v-shaped or rapid recovery as state economies open up, it seems unlikely that demand approaches pre-pandemic levels any time soon. Ethanol production holds a strong potential for a more u-shaped or gradual recovery under any gasoline demand scenario.

Ethanol production for the remainder of the marketing year holds numerous complications due to the uncertainty in the economy. This projection assumes a gradual but sustained return of economic activity through the summer leading to an expansion of gasoline consumption. A few more weeks of lower production seems inevitable. After the initial weakness, a gradual recovery brings production near 740 thousand barrels per day (approximately a 30 percent reduction from last year) through June and 860 thousand barrels per day (roughly a 17 percent reduction from last year) for the remainder of the marketing year. Corn use for ethanol for the marketing year under recent conversion rates comes in near 4.750 billion bushels, 300 million bushels lower than the current forecast.

A portion of the losses looks to be offset by increased feed use, but not enough to prevent a substantial increase in corn ending stocks. Despite substantial reductions in distiller's grain production, the gain in corn use for feed pales in comparison to the losses from lower ethanol production. Disruptions to supply chains continue to punish livestock producers. Cattle feeder placements look to move lower under the pressure through summer. Lower fed cattle margins, even with lower feed costs, may limit buying feeder cattle. The short-term outlook for hog markets remains bleak as finished hogs back up into the countryside. At present, hog slaughter capacity sits down 25 percent. Sustained issues for hog producers may see production lower in the second and third quarters. Broiler eggs set saw two consecutive weeks of five percent lower levels from last year. Across the board, livestock production appears to be pulling back under the circumstances.

Hopes for a rapid economic recovery hinge on increased economic activity that seem many weeks into the future. A morbid calculation pitting economic pain against loss of life continues to come into focus and enter the political discourse. Barring the rapid development of a vaccine, expanded testing, or successful treatment, the economic losses will continue to grow. Ending stocks for corn this marketing year look to move higher and corn prices will reflect this reality.

YouTube Video: Discussion and graphs associated with this article available at:
https://youtu.be/6toW_kkCtY4