



Weekly Outlook: Revisiting Corn Use for Ethanol

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Stronger export numbers and lower acreage boosted corn prices since the end of June. Concerns about demand weakness in ethanol production emerged recently. A recovery in economic activity helped ethanol plants ramp up production as gasoline demand increased. A resurgence in virus incidences threatens ethanol production over the short run and injects uncertainty into long-run prospects.

Gasoline demand recovered to almost 89 percent of pre-coronavirus lockdown levels in early July. Despite this positive development, the recovery in demand flattened out over the last few weeks. Gasoline stocks began to recede but still sit substantially above levels seen at this time of the year. Attempts to reopen the economy hit a snag as the virus spread rapidly around the country after initial hopes saw a rapid opening in many areas. At 8.648 million barrels per day, demand recovered substantially from the low point of 5.311 million barrels per day seen in early April. The path back to normal gasoline demand levels appears stalled. Ethanol production followed this recovery and will feel the implications of flattening gasoline use.

Weekly ethanol production increased for the twelfth consecutive week according to the EIA ethanol production report for July 10. Since April 24, ethanol production increased by 394 thousand barrels per day to reach 931 thousand barrels. Current estimates place production capacity near 88 percent of normal. Ethanol stocks fell to 20.6 million barrels from the record-high 27.7 million barrels recorded on April 17. Ethanol production leveling off over the next couple of weeks, as gasoline demand plateaus, appears likely due to an uptick in coronavirus issues in states in the South and West. If production does slow, it places the current estimate for corn use in question. Expanded exports could help the situation.

Ethanol exports saw a drawback as the world locked down. Through May, ethanol exports sit behind last year's pace by 51 million gallons. If this pace continues through the end of August, ethanol exports will see a second consecutive year of declining totals from the peak of 1.632 billion gallons during the 2016-17 marketing year. Lower exports to Brazil, India, and the Philippines hurt the pace this year. Declining Brazilian exports seem inevitable and look to continue as they build expanded domestic capacity. The current pace places ethanol exports near 1.5 billion gallons for the marketing year. A resurgence of Chinese buying, as seen with other agricultural products recently, holds some hope. Over the last five marketing years, China's maximum U.S. ethanol purchases totaled 208 million gallons in 2015-16.

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USDA dropped corn use for ethanol in the July WASDE report by 50 million bushels for this marketing year, down to 4.95 billion bushels. The current estimate for corn use remains feasible. Through July 10, if the corn conversion rate seen in recent months extended into July, corn used for ethanol sits near 4.14 billion bushels. Over the remainder of the marketing year, the USDA estimate requires an additional 706 million bushels of corn use. At recent conversion rates, this estimate requires approximately 953 thousand barrels per day of production for the remainder of the marketing year. The present estimate sits above recent production levels and hints at the possibility of slight further reductions in USDA's corn use numbers. The magnitude of an adjustment at current production rates indicates a 10-15 million bushel drop for the current marketing year. A significant issue is what a continued resurgence means for next marketing year corn use.

Ethanol production for the next marketing year contains a massive amount of uncertainty due to the current economic outlook. At present, the USDA forecasts corn use for ethanol at 5.2 billion bushels in 2020-21. A forecast of this magnitude signals a drop of about three percent for the entire marketing year off of recent use levels unaffected by the economic shock. The Energy Information Agency, in the July short term energy outlook, projects ethanol production at five percent lower than pre-coronavirus production levels over the next marketing year. After initial lower production levels on par with current totals, a gradual recovery brings production near one million barrels per day (up from 710 thousand barrels in 2020 and down from 1.05 million barrels in 2019) through the second quarter of 2021. An expectation of slight increases covers the remainder of the 2020-21 marketing year. Corn use for ethanol for the 2020-21 marketing year under recent conversion rates comes in near 5.1 billion bushels under EIA assumptions, 100 million bushels lower than the current USDA forecast. The difference between the two projections is not insubstantial.

Improving weather prospects and uncertainty about the economic outlook holds the key to corn price developments over the near term. The importance of ethanol as a corn demand source remains crucial. As we move into the next marketing year, economic activity needs to improve to maintain this fundamental driver of corn prices.