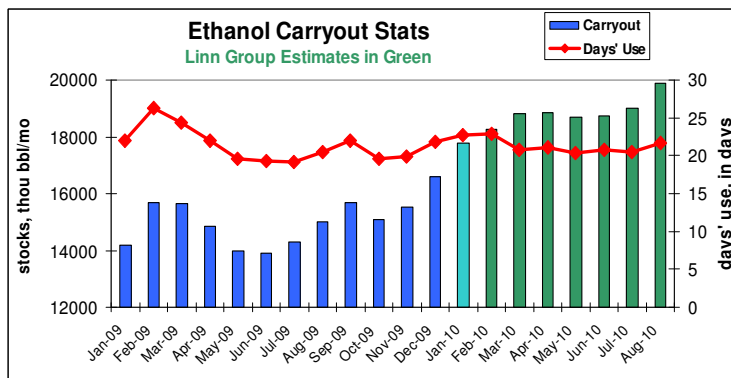
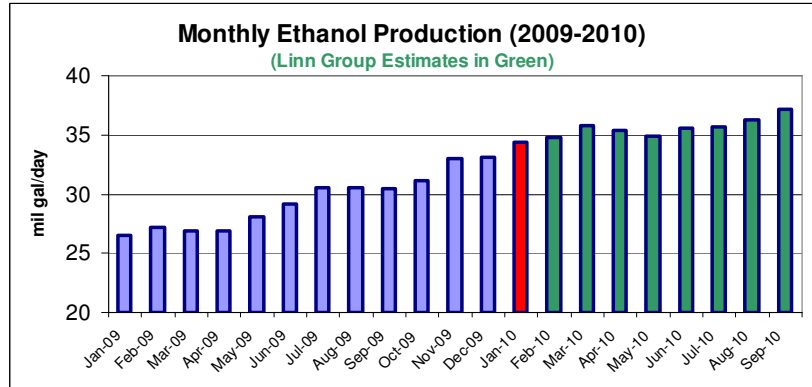




## The Linn Group Ethanol Wire – 4/13/10

EIA's Monthly Ethanol stats for the month of January were notable, setting all-time highs for monthly production, disappearance, and carryout. In terms of the broader trend, little has changed. Ethanol output continues to outpace consumption, leading to a sharp expansion in ethanol carryout.

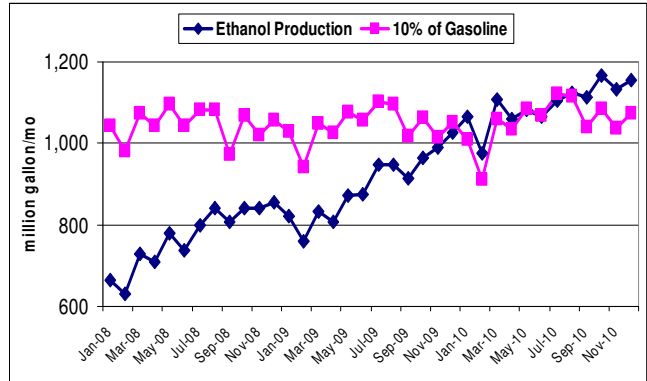
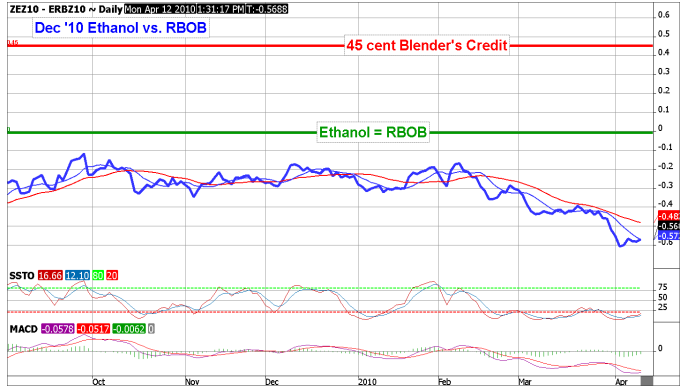
EIA statistics estimate January ethanol production at 1.065 billion gallons, an increase of 3.9% from December. These gains were slightly higher than forecast, as cold weather in Jan boosted ethanol yields at many locations. Ethanol consumed roughly 370 million bushels of corn in Jan. We also saw another 200 mil gal/yr of capacity restart, including a 100 mil gal/yr plant in PA. More scheduled plant re-starts (three from Valero alone) and cold weather should continue to promote strong gains in ethanol production through early spring. The deterioration of ethanol profitability that began in March may prompt an extended maintenance period in April & May, which will offset some of these capacity gains, and should interrupt six consecutive months of monthly ethanol output expansions. A number of large plants are due to begin production this summer, which will once again promote a gradual expansion of ethanol production, renewing a push to new record highs. Our estimates of 09/10 ethanol corn use remain at 4.4 billion bushels, 100 million bu above the latest USDA update in April.



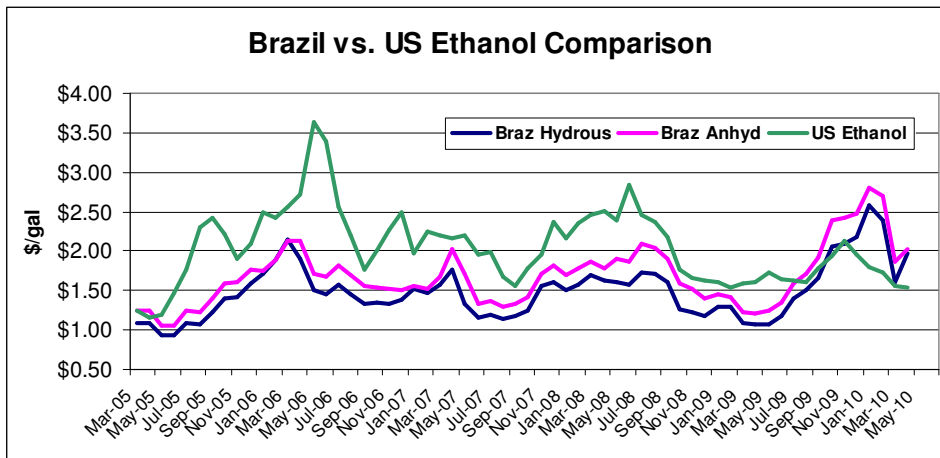
Spring maintenance will not come too soon, as ethanol carryout has exploded since autumn. The EIA reported ethanol stocks hit 748 million gallons in January – a new record high. Carryout should continue to build through March, as reflected by relatively soft ethanol cash market pricing and futures deliveries seen recently. Ethanol storage space is relatively limited; many plants had to price ethanol at a discount, depressing cash values. At March levels, carryout should see a quarter or two of relative stability until summer production increases become too much for use to keep in check.

Ethanol disappearance in January also achieved a new record high, reaching above 1 billion gallons for the first time. Imports of ethanol into the US remained at extremely low levels – only 1.4 million gallons. Jan was the third consecutive month where ethanol exports exceeded imports, helping to soak up some of the US supply. Net US ethanol exports should continue in the near term, as low US prices relative to world values prevent imports and promote limited export business.

The 10% blend wall almost certainly influenced the January ethanol stats, limiting discretionary blending opportunities and pushing ethanol into storage or discount channels. Despite record disappearance, EIA data indicates blender ethanol consumption fell from Dec. Fortunately, the blend wall issue will be somewhat relieved by summer gasoline demand. Weekly data from the EIA indicates monthly US gasoline demand bottomed in January. Refiners have since picked up run rates, anticipating the seasonal increase in demand that inevitably comes with warmer temperatures and summer vacations. With ethanol blending returning over 10 cents/gal variable profit through Dec 2010 (even more up-front), blenders will jump at any opportunity to push more ethanol into the system.



The blend wall issue, however, will become a greater factor in the latter half of 2010, due to a renewed summer expansion in ethanol production, unless the EPA blesses E-15. Even if the EPA does take positive action on the issue, liability concerns from retailers, car manufacturers, and other involved parties may limit immediate adoption. A number of spec houses are actively betting the EPA will raise the blend limit. Buying Dec Ethanol and Selling Dec RBOB Gasoline emerged as an active trade last Tuesday. It is estimated 500 to 600 contracts of the spread took place that morning, and led to a greater than 50% expansion in Dec ethanol futures open interest.



Brazil ethanol values firmed over the last two weeks. E-95 (hydrous) ethanol has rallied 30 cents off March lows, trading last at \$1.98/gal. It's interesting that the anhydrous (E-20) move has been much less dramatic, improving 15 cents off the lows to \$2.03 a gal. This may be an indication of two things. First, supplies of anhydrous ethanol may be building ahead of a move back to a

25% blend. In January, the Brazilian government reduced the effective blend rate in regular gasoline to 20%, from 25%, saying it would be for a 90 day period. We're rapidly closing in on that expiration.

Second, retailers in Brazil may finally be passing ethanol price declines on to E-95 consumers. There were reports of enormous spreads between ethanol plant prices and E-95 prices at the pump. Price declines would likely rekindle growing demand for E-95 in Brazil.

Brazil's trade commission announced last week they would suspend the country's 20% ethanol import tariff, effectively immediately and lasting until the end of 2011. How convenient. Brazil rejected a similar move in February at the height of the cane crunch, when ethanol supplies in the country were restrained. Brazil is obviously angling for the US to do the same; the US import tariff expires Dec 31.

There is nothing new to report out of Congress, as they have just returned from a two week long Easter recess. Bills that include the \$1/gal biodiesel tax credit, a multi-year extension of the ethanol tariff and tax credit, and a bill that would provide an 80% loan guarantee for an ethanol pipeline project all remain circulating. A couple of political contacts have implied there was yet another significant delay on the bill containing the \$1/gal biodiesel credit – but this remains unconfirmed.

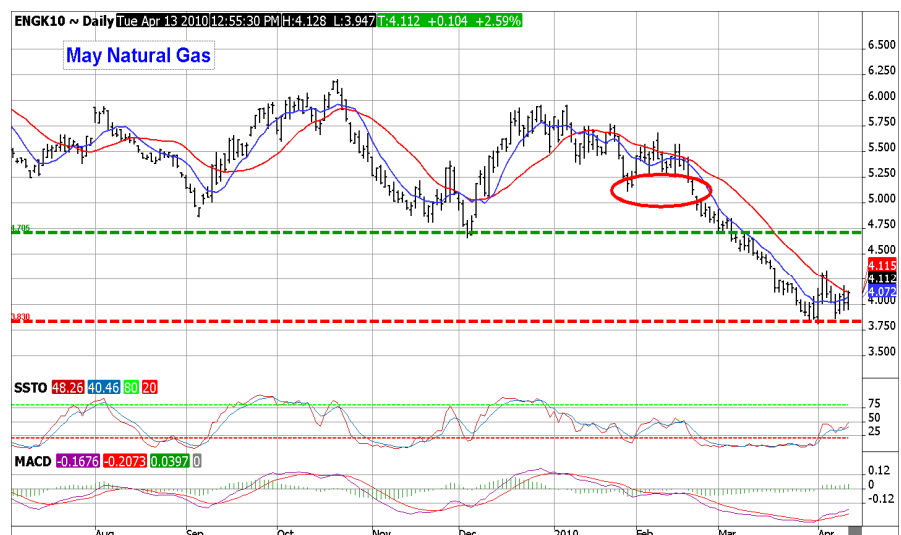
Over the recess, the usual suspects – Grocery Manufacturers Association, American Meat Institute, etc. – were aggressively lobbying against the ethanol tax credit extension. In an effort to help counter this influence, ethanol trade group Growth Energy announced they would fund a television ad campaign to help educate the public about the benefits of ethanol. The public relations offensive, which will run for 12 weeks and cost \$2.5 mil, will be spread across the major cable news networks. Half of the ads will run in prime-time. Ethanol giant Poet also announced a separate \$3 mil ad blitz. The TV ads can be viewed here: <http://www.growthenergy.org/news-media-center/broadcast-media/americas-fuel-campaign/?/ads>.

The new EIA statistics due out in the Jan ethanol stats release were relatively disappointing. The first count of E-85 production stats show only 714,000 gal in Jan. For a comparison, consumption of E-85 in 2007 amounted to 51 million gallons, or an average of 4 mil gal/mo. E-85 pump availability has expanded greatly since 07. Contacts at the EIA say E-85 is almost certainly under-reported, due to data collection methods. Most E-85 is blended downstream from EIA survey respondents.

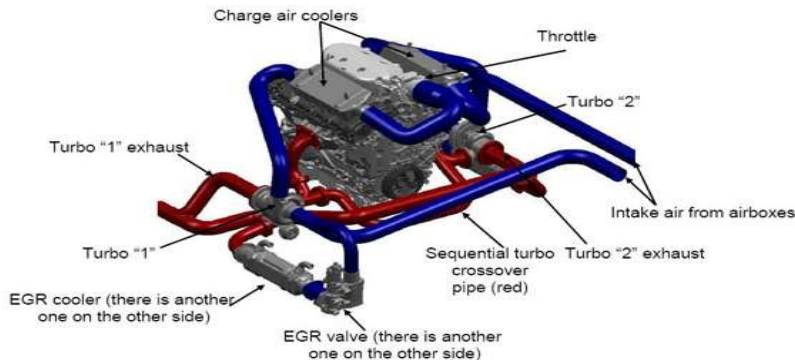


The ethanol market saw calendar spread widen out again, with the May-Dec carry expanding back out to 9 cents. Deliveries against the April contract applied pressure to front month contracts last week; CBOT reported 310 deliveries total. However, pressure from deliveries should subside as we move through April, and concerns over spring maintenance may begin to support prices. Brazil ethanol has also ceased to be a negative drag on US values. A big support shelf at \$1.45 and \$1.50 in ethanol futures looms just ahead.

May Natural Gas appears to be trying to make a good trade, after attempting to push back down into support below \$4. We think this kind of price action likely makes \$4 to \$4.25 a significant value area for 2Q natural gas needs. The market remains on a fairly negative fundamental footing, but the market is currently leaning too far short, with large discretionary fund short open interest building. Multiple layers of resistance in the \$4.75 to \$5.25 area should hold this rally in check. The natural gas market will be closely watching the Industrial Production report Thursday morning for a hint on commercial demand; later on the same day, the EIA is expected to report a +60 bcf inventory build.



In other ethanol news, as a reminder, April 26<sup>th</sup> marks the launch of the CMEGroup's new DDG futures contract. May 1<sup>st</sup>, Illinois will become the first state to enforce new quality standards related to the performance of ethanol-blends, as outlined by the National Conference on Weights & Measures. The new standards will move ethanol blends more in line with conventional unleaded in quality, performance, and additives. This may lead to a small increase in the price of gasoline, as refiners will have to ship and store gasoline for ethanol blends separately.



Gilbarco Veeder-Root became the first major company to announce they have upgraded existing fuel dispenser warranties to cover E-15. A report published in the mainstream media touted EBDI technology as a potential way to address new fuel efficiency requirements of 35.5 mpg by 2016. EBDI is an engine specifically optimized to take advantage of ethanol's unique chemical properties – and is similar in technology and efficiency to diesel engines.

Minnesota Energy said they were indefinitely shutting their 20 mil gal/yr ethanol plant at Buffalo Lake, MN. The company's other grain handling operations will not be affected. The MN Energy plant was the smallest in the state – some talk it may be converted to produce food-grade alcohol. Minnesota state government announced they were cutting ethanol producer payments by \$4.5 mil - \$7.6 mil remains. Canadian province of Manitoba going the other direction, saying they would begin offering direct producer payments to encourage biodiesel production. Manitoba will offer 53 cents/gal, capped at 5 mil gal/yr – the province has three plants with capacity between 4-5 mil gal/yr.

Iowa-based Renewable Energy Group announced the temporary idling of biodiesel plants in Ralston & Newton, as the fate of the biodiesel credit remains in limbo. Pacific Ethanol reported a gross 4Q profit of \$1.4 mil, excluding a \$250 mil impairment to adjust for updated valuation of their ethanol facilities. Pacific's earnings report noted if they end up surrendering control of their physical plants to lenders, Pacific will earn fees/incentives for managing the plants. South Haven, MI city council still considering whether to allow DeAnza to spend \$6 mil converting a Detroit piston plant into a sugarcane ethanol mill. Aventine distributing new common stock shares pursuant to reorganization plans. Great Western Ethanol's proposed 112 mil gal/yr corn ethanol project in Colorado officially declared dead.

Bunge is planning to spend \$750 million to expand capacity at three Brazilian cane ethanol plants, as part of their broader initiative to push their total cane crushing capacity to 30 million metric tons (mmt) per year by 2012. By June, Bunge's Brazil cane crushing capacity will stand at 20 mmt, after Moema acquisition for \$1.5 billion is finalized. Louis Dreyfus is bidding with Cosan & Bunge for 35 mil gal/yr Usina Mandu cane ethanol plant. State-controlled Petrobras firing up their first cane ethanol plant in Bambui. The Bambui plant will produce 25 mil gal of ethanol per year, and is part of their own longer-term plan to expand ethanol production to 1 bil gal/yr by 2013, spending about \$2.8 bil.

A 10 mil gal/yr cassava ethanol plant Project in the Philippines was halted, after the company could not secure environmental clearance. Uganda may invest \$100 mil in sugarcane ethanol production, if the government approves a national blend mandate. The largest oil refinery in Thailand setting aside \$30 million to buy an ethanol plant in the country. An Indian business paper claimed 99% of biodiesel production in some areas of the country has closed. An industry report found German biodiesel blending rose 41% in 2009 to 667 mil gal, but high taxes at the pump led to a 78% fall in direct biodiesel sales to only 70 mil gal. The result was a net 53 mil gal reduction in biodiesel use.

In technology, Great River Energy is reportedly moving forward with plans to build a \$300 million 20 mil gal/yr cellulosic ethanol plant in Spiritwood, ND. The cellulosic plant would be co-located with a coal-fired power plant and would be complete by 2015. Concurrent plans to build a corn-based

ethanol plant at the site were cancelled. American Energy Enterprises developing a project to construct a 15 mil gal/yr cellulosic ethanol plant in New Milford, CT. AEE claims their cost to produce cellulosic is 80-85 cents/gal, with production expected to start in late 2010.

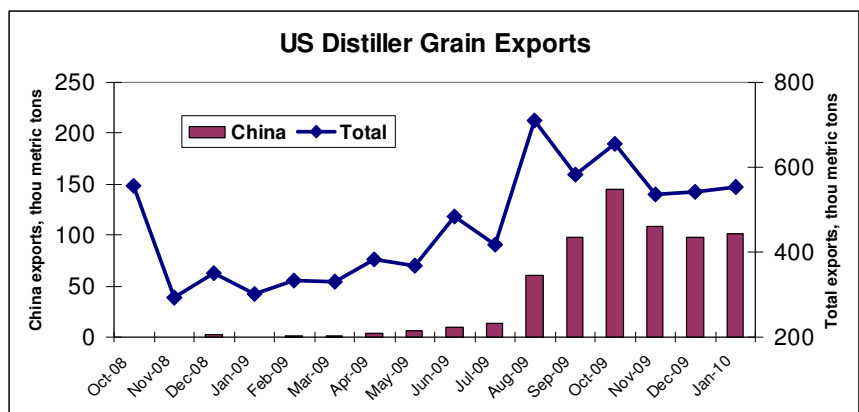
The Dept of Energy announced two new grants/partnerships: lab at Lawrence Berkley will receive \$18 mil to build Advanced Biofuels Process research facility, and partner with GM to study jatropha biodiesel in India. Next generation sugarcane ethanol producer Amyris received \$48 mil in funding from Singapore based Temasek holding. Cash-strapped Verenium & BP announced they would extend their partnership for four more months, under the terms of the deal, Verenium receives \$2.5 mil per month. An industry group is touting sorghum as a cellulosic feedstock, saying energy/acre is better than switchgrass and sorghum uses less water than comparable cellulosic feedstocks.

A KSU research piece criticized cellulosic ethanol made from crop residue, saying the practice strips away vital soil nutrients. Verdezyne teaming up with Lallemand Ethanol Technologies in an effort to improve ethanol yeast efficiencies – the project is expected to be complete by 2012. Schneider, IN trash-to-ethanol project moving one step closer to reality, after the city council agreed to a profit-sharing agreement with prospective plant owner Powers Energy One. An official French government report supported the use of land-use change in biofuel greenhouse gas calculations. A UK gov report concluded biofuels were NOT to blame for the 2008 food crisis (drought and \$100+ crude were).

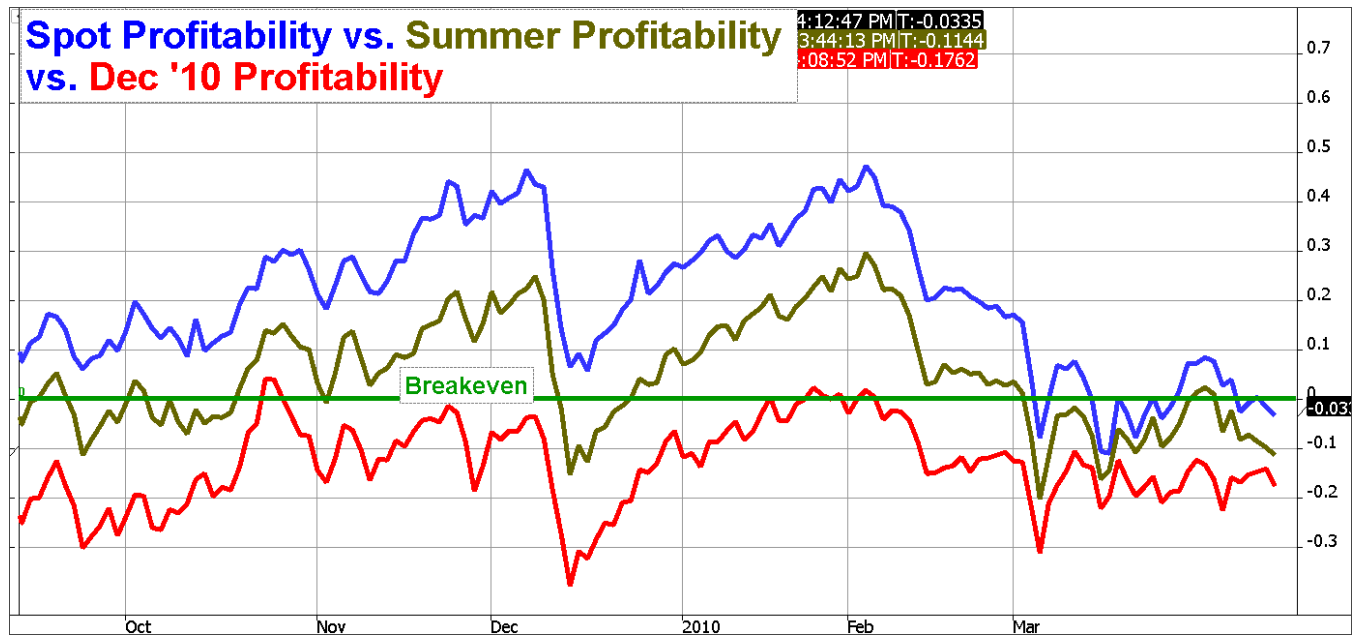
DDG Table						
	Today	Last Week	Last Month	Cash Corn	% Cash Corn	Lst Wk %Corn
Iowa	\$95	\$90	\$100	\$3.30	81%	76%
Illinois	\$105	\$100	\$112	\$3.40	86%	84%
South Dakota	\$93	\$90	\$100	\$2.90	90%	84%
Nebraska	\$95	\$93	\$101	\$3.30	81%	79%
Nebraska Mod DG	\$45	\$40	\$50			
Nebraska Wet DG	\$35	\$34	\$37			
*All Distiller Grain values in USD/ton						
Brazil Hydrous Ethanol	\$1.980	\$1.610	\$2.002			
Brazil Anhydrous Eth.	\$2.026	\$1.870	\$2.397			
Ethanol Futures OI	8,589	7,895	8,280			
Ethanol OTC OI	48,919	52,418	52,517			

(OI = Open Interest)

Distiller grains are a distinct bright spot for ethanol this week. DDG trade at the Gulf popped \$5 to \$7 a ton on Friday, after reports surfaced that China bought 200,000 tons of US DDG's. Exports have done a great job of soaking up extra DDG production, as the ethanol industry has greatly ramped up operations over the last six months. Prices firmed in response to robust export business – Illinois plant values rallied above \$105, despite a lower corn board. Other locations firmed noticeably relative to cash corn as well. DDG prices could be the ultimate benefactor if ethanol plants take an extended maintenance period this spring. Domestic livestock producers may attempt to reach out for DDG's in the deferred to mitigate the risk of an ethanol industry slowdown – or to lock-in improving livestock profit margins. Ethanol byproducts have gone from a drag on profitability in March, to a slight positive factor now.



Average Midwest ethanol margins remain right around breakeven. Plants are reportedly having an easier time moving ethanol now, compared to last month, due mostly to the seasonal expansion in crude refining capacity. Carries in ethanol and carries in corn/natural gas roughly offset each other, preventing the establishment of positive forward margins at this time.



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