Research

Monthly Sugar Note

30 December 2022

Markets

Year 2022 had started with markets looking forward to a post COVID era. The arrival of vaccines and the easing of lockdown measures around the globe led to an early sense of optimism. But as world demand returned, the pandemic-induced supply chain delays took longer to recover, generating a wave of inflation everywhere. Complicating matters, a war broke out between an important energy player and a big grains supplier. Centrals banks acted by increasing rates to control price gains, while some countries set exports bans leading to extreme volatility in commodities.

Markets watched the US Federal Reserve like a hawk, whose actions supported the USD higher, causing other currencies, equities, and commodities to weaken. But as other central banks raised rates, and US inflation began to peak, the dollar's ascent has since been halted. For macro, 2024 will be a year of transition with most economies still struggling to deal with the post Covid costs of inflation, rising interest rates and growing risks of recession.

Sugar prices averaged 18.8c/lb during 2022. The lowest point, at 17.7c/lb, was at the end of July when Brazil was near the peak of its harvest, while the highest price was observed in the past weeks when the market reached 20.6c/lb, the highest in 6 years. 2022 started with a record Indian crop along with a small recovery in Thai production, and Brazilian mills prioritising ethanol production with lower cane yields given the dryness in 2021. With the help of the Brazilian government's reduction in fuel prices and the strong global demand for whites, C/S mills switched their focus towards sugar production in the second half of 2022.

Figure 1: NY11 front month in 2022

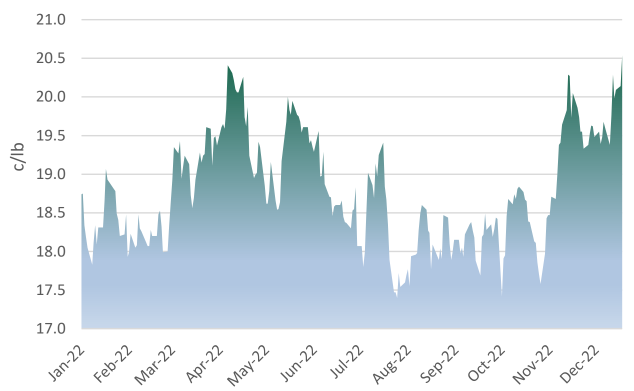
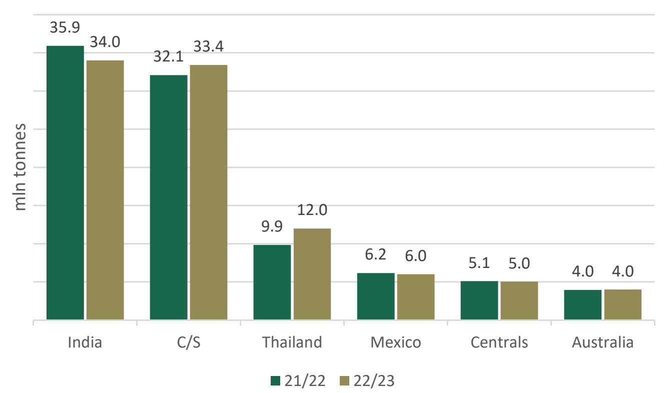


Figure 2: Main players' sugar crops (crop year)



Source: Bloomberg and ED&F Man Commodity Research

2023 starts with high expectations for the next Brazilian crop which will turn the global SnD into a surplus. India should see production decline from last season and Thailand is consolidating 2 digits in its sugar output figures. The other major suppliers (Centrals, Mexico and Australia) should see similar production figures to last year. Yet prices are well supported. The market is currently unsure who will fill the gap of the lower Indian exports and, more importantly, what will be the size of that gap. Let's not forget that India exported close to 11mmt last season, whereas it may not have more than 8mmt this season, even in the best of the cases. Consequently, we are watching the development of the Indian crop to foresee additional export quotas and the real size of the Thai crop which, as history has taught us, can change quite abruptly in the last months of the harvest period. In the meantime, supportive weather for Brazil and high sugar prices suggests a very sugar-oriented crop for the C/S millers in 2024.

The market also understands that the surplus projected in 2024 will only shows its face when C/S Brazil's 23/24 crop reaches its peak in the second half of the year. But given expectations of record grains crop exports by June 2024, there will be immense competition for space with sugar in Paranagua and Santos. All in all, the sugar market will be navigating in tight conditions in the New Year and any negative signs in the three big producers of the market can take this market to very high levels.

Fundamentals

- **Brazil C/S:** November production results were extraordinary and resulted in revisions giving strong crush numbers and higher than projected ATR as well as sugar mix. With that, the projections for the season have increased to 33.5mmt of sugar with 45.7% of sugar mix, a growth in mix of 0.8p.p. YoY. Given the agricultural yields registered so far, CS could crush even more cane than our current projection of 548mmt, but the wet 1H of December might have led more mills to finish their season earlier, a point that will be clarified at the next UNICA report. On the other hand, these rains were good for next year's cane development, which continues to suggest cane of 584mmt and sugar production of 36.2mmt with a 46.5% sugar mix. Exports are starting to slow down, but are still at a relatively high pace for this time of the year, and December should register almost 2mmt of exports.
- **India**: In the current 2022/23 season, India's crushing operation is at full pace, with around 490 mills operational. They have produced 8.2 mmt of sugar up to 15th Dec 2022. Based on our crop surveys we are estimating 32.4 mmt sugar production, -9.7% lower than last year, basis lower agri yields following initial lower rains. In June the grand growth phase of the crop, and then continuous heavy rains, cloudy weather, and waterlogging conditions, negatively impacted cane growth. The realized harvested yields are coming lower than last year, and we could see a lower crushing pace from 1st half Feb onwards. Based on the crop tour findings we are estimating Maharashtra sugar production to be 11.26 MMT vs 13.72 mmt last year and in Karnataka 5.29 vs 6.1 MMT last year. Out of the 6 mmt export quota so far, around 5 to 5.4 mmt of sugar has been contracted. On a monthly basis, 913 kmt were exported up to Nov 30th, 2022. Looking at the heavy nominations we are estimating around 900 kmt in Dec 2022 and a balanced quantity of exports will be estimated majorly in Q1 2023.
- **Asia**: December saw the start of the Thai crush which was slower YoY due to the late crush start date for the Central region which should begin in the New Year. Despite this, the regions that had begun crushing saw quite good progress, which is encouraging. The ban and penalties in burnt cane is also reflected in higher sugar yields so far in the crush and should support overall sugar production. On the demand side, Indonesia's demand continued to be strong with more import permits given for November and December which is showing up in the line-ups, although the high flat price may discourage some to import. On the refined space, flows continued to be strong in November into the border regions of Thailand which is still seeing good demand for now. Overall, new crop Thai cash prices are still high except for the nearby shipment windows due to the high NY spreads which is representative of overall global tightness unless we see more Indian sugar come to the market.
- **US:** The December WASDE had very few updates for the US SnD. A small decrease of 43k MTRV in production was seen, but this was offset by an increase of similar amount in the Mexican quota to keep STU unchanged at 13.5%. According to the current Suspension Agreement, 80% of the 1340k MTRV (1264kt tq) reported as Mexican quota are now guaranteed, but the evolution of the SnD and high duty imports until March can have important effects on the final quota.

- **Mexico:** The 2022/23 crop started in early November, with delays in terms of day and number of mills running when compared to the planned schedule. With that, the initial results released by Conadesuca can be misleading as the sample and number of days running are quite different. Regardless, up to December 3rd, cumulative sugar production has reached 162kt vs 236kt last season. These initial results are due to the poorer agricultural yields and sucrose levels, which can be a flag for a lower crop compared to the past season which ended at 6.2mmt.
- **Centrals:** Most of Centrals' mills have already started their crops. The outlook for the current crop is close to 5.0mmt, with a small reduction YoY. In El Salvador, the crop started on average 5 days later than usual and sugar production up to Dec 11th reached 73kt vs 128kt at the same period last year. Guatemala also had a very small delay on average, and up to Dec 3rd has already produced 306kt of sugar vs 364kt in the past crop. If production is a little slow, exports on the other hand are busy, with many nominations for bulk raws and refined sugar already happening.
- **EU:** A cold snap in December is likely to have delayed the back end of the harvesting, as rock hard soils make it difficult to remove beets from ground. Temperatures are warming up this week, which should give farmers the opportunity to continue. We have recently reduced our production estimates for EU27+UK by 100kmt to 15.9mmt (on a commission methodology). In our trade figures, we saw 55kmt of Ukraine exports to EU in November, above the logistic capability estimate for one month, leading us to increase our overall whites import number for the year.
- **CIS:** The main change made during the past month is our Ukraine production estimate, which has continually surprised since the invasion in February – output has been increased by 200kmt to 1.3mmt. at the same time, we have reduced our consumption estimate by 100kmt to 0.9mmt. As a result, we see additional export capability, of which we expect most of the surplus to go to increased stocks.

Focus – 2022 overview and expectations for 2023

- **Brazil C/S:** 2022 was another very challenging year for CS Brazil. Although the cane fields presented an important recovery when compared to the previous year, the economical volatility and political interventions had an important effect on the profile of fuel consumption and consequently production mix. On the agricultural side, cumulative yields up to November were 9.2% higher YoY, resulting in significant growth of cane. The latter begs the question now on whether there is time available to crush, as some of it might end up being processed in April in the new year. Still, recovery on yields is important for the medium term as well, as it can impact the following crops. The final crush depends on weather from now until end of Q1, but should be close to 548mmt and sugar production close to 33.5mmt, a 1.4mmt growth YoY. The major changes are related to political factors this time. The production mix in the first few months of the season were more sugar oriented but very far from max sugar levels as hydrous demand was high following extremely high gasoline prices due to the weak BRL and high oil prices last quarter. As a result, important political changes - a reduction in state taxes and the removal of the federal taxes until the end of the year – led to a substantial drop in gasoline prices and shifted consumption towards it. With that, the sugar advantage over ethanol increased, and from June onwards millers shifted to maximise sugar as much as possible, boosting sugar production. Sugar exports were also high, with strong demand and good performance at the terminals, supporting Brazilian cash levels throughout the season. The improvement on the cane fields registered in 2022/23 is already a big start for the 2023/24 production, and good weather along all the major development periods will be important to provide even better results. September and October had very good rains, but a dry November raised a flag. Still, the return of good volumes in December so far, and satisfactory forecasts, indicates positive conditions ahead. Weather will be monitored very closely, but as of now we estimate 584mmt of cane and 36.2mmt of sugar - as based on current prices, it should be a max sugar crop. The production mix though will probably be a major point of interest for the year ahead, as many political decisions can take place which will have implications on it. In 2023 Brazil will have a new president, the former president Lula, and the local currency could face high volatility with potential concerns about populist measures and adherence to the fiscal budget. It's not clear if the federal taxes on fuels will return, but some sort of measures to keep gasoline prices down are expected, either by taxes or more direct interference at Petrobras. In this scenario, hydrous demand should once more weaken, pushing mills to focus on sugar production. This would take it almost 3mmt higher YoY, resulting in another year of strong exports.

- **India**: Last season saw India as the star performer, with record production and huge exports that helped offset losses in other key producing regions. In the 2021/22 season India produced 35.9 MMT of sugar and exported 11.1 mmt of sugar, around 5 mmt were exported as bulk Raws and 2.6 mmt refined, 3.4 MMT of LQW sugar. For the 2022/23 season, as highlighted earlier, we have just recently concluded a comprehensive crop survey in India. The results lead us to estimate India's sugar crop at 32.4 mmt, nearly 10% lower than last year, due to lower agri yields following initially lower rains. In June, the grand growth phase of the crop, and then continuous heavy rains, cloudy weather, and waterlogging conditions, negatively impacted cane growth. The realized harvested yields are coming lower than last year and we could see a lower crushing pace from 1st half Feb onwards. Our outlook for the 2023/24 season is expected to be slightly higher YoY, looking at the water availability in reservoirs. Farmers' intentions towards cane planting are positive because of better returns, compared to other crops. In addition, we have a higher plant proportion for next season which will be a positive factor that will allow better agri yields or cane, YoY. With the maintained acreages and assuming a normal monsoon with normal agri yields, our very early estimates are for 33.27 MMT of sugar production for the 2023/24 season.

Figure 3: Production changes (21/22-22/23 Oct-Sep)

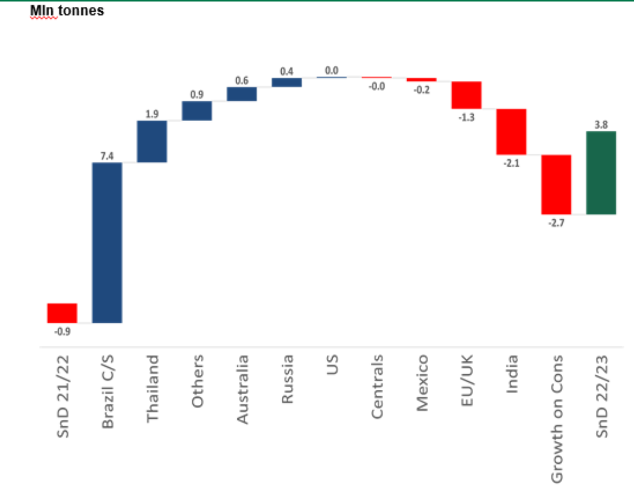
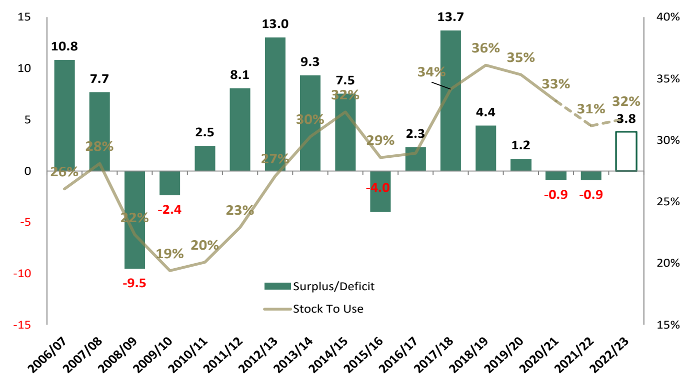


Figure 4: World sugar market SnD (Oct/Sep)



Source: Bloomberg, ED&F Man Commodity Research

- **Asia:** 2022 has been a year of tightness for the region with raw premiums trading over 200pts and whites often over $50 despite a recovering Thai crop of 92mmt cane vs the prior disastrous years of 19/20 and 20/21, at 74mmt and 66mmt cane respectively. The reason for this is mainly due to strong regional demand for both qualities after most countries came out of Covid lockdowns with consumption recovering. When combined with poor crops in specific regions like Vietnam and Philippines, there was always a strong bid for sugar. Moreover, extra-regional demand for Thai refined was also strong at about 400k from deliveries, which supported cash premiums. Another important factor was high freight rates earlier in the year which meant that Thai cash had a strong freight advantage, further supporting elevated premiums. Chinese demand was surprisingly strong despite negative margins for most of the year as refineries worried about losing their OOQ allocations for next year. Looking forward to 2023, the Thai crop is expected to further improve to 105-115mmt cane with very good rainfalls during both the planting and growing periods of cane, although slightly dampened by competition from cassava. In a world that needs sugar desperately and with regional import demand expected to improve further, it's not difficult to see outlets for Thai sugar despite higher production. It will be interesting to monitor for the potential for further crop upside as well as white premiums, which would determine the preferred quality of produce for mills. On demand, China looks to be amply supplied but with the reopening and a slightly poorer crop outlook, there may be some cause for continued import levels. But refineries margins and their preferences to import need to be closely monitored.

- **US**: The 2021/22 season produced 8288k MTRV, which represents a fall of 1.1% YoY. Despite this drop, the level of production is a relatively good result for US, even if it wasn't evenly distributed - cane was down 3.9% YoY while beet was 1.2% higher, the second highest ever for beets. On top of the overall lower production YoY, domestic deliveries had a 2.4% growth which kept domestic prices very high and incentivized imports, even paying full duty. Although the stocks levels indicated a S/U ratio of 14.3% by end of Sep, which is above the theoretical balanced level of 13.5%, the uneven distribution of this sugar, some logistical challenges along the year and low feedstock for all the refining capacity, kept prices at a high level. The current new crop already starts under challenging conditions and we expect it to reduce by another 1.1% to 8199k MTRV. However, this time with a 4.4% cut on beets and a 3.3% improvement on cane, which includes a record high for Louisiana. The feeling of tightness in the market, lower production and good demand are ingredients for elevated prices and high imports ahead. Mexico has good availability to supply import needs but before the final quota gets released by March 2023, large volumes of high duty sugar will probably be imported. This should offset part of the need for this quota, limiting the potential for Mexican imports and keeping prices high.
- **Mexico**: Ever since the big production shock in 2019/20, the Mexican sugar industry has slowly recovered and in 2021/22 it got back to good levels of production, registering almost 6.2mmt - a growth of 8% YoY. This was a consequence of good agricultural yields and the second largest acreage ever harvested in Mexico. The good crop resulted in a season with minimal imports and good availability for markets as IMMEX, which had a record of above 500kt supplied from the local mills. Good domestic sales allowed sugar to increase its share over HFCS, yet it still had the ability to provide around 1.15mmt to the US market while still exporting above 500kt to the WM. The crush of the 2022/23 season has recently started and the weekly production reports will be an important tool to measure the crop performance and overall export availably. As mentioned, this season the United States will likely need a relatively high Mexican import quota. The beginning of Mexico's crop had a delay, and the initial results are still inconclusive, but given the irregular rainfall registered along the year, it's expected that the crop presents a YoY reduction. Market projections are for a crop of 6.02mmt which represents a 3% drop YoY and a break in the recovery pattern Mexico has had in the past two years. The current projection of US quota of 1264kt would result in WM exports of around 200kt. However, any further cuts in production would be removed from this amount, so in general it should be a year of small volumes of Mexican WM exports.
- **Centrals:** The 2021/22 season finished with a recovery of around 6% in terms of sugar production when compared to the poor performance of the previous season. Out of the approximately 5.1mmt produced, around 2.9mmt were exported as bulk raws, refined, bagged raws and LQW. The better crops registered in other origins, especially Thailand, has reduced the Central's competitiveness in Asian markets, creating a regional surplus for most of the crop year. Favourable weather conditions during the season's cane development have supported the projections of production at levels relatively close to last year's. Despite a very wet year, the lack of any major weather event has helped the cane fields. Still, the region should report a reduction of around 1% YoY, with sugar output at good levels of 5.0mmt. Different from a year ago, the demand for Centrals' sugar is already very heated and should continue at a good pace over the course of the season, while sugar lasts.
- **EU/UK**: After the 2020/21 season's crop failure that saw stock levels fall to extreme lows, the 2021/22 crop made a 2mmt recover. However, net trade and a rebound in consumption led to a smaller stock increase than was necessary to return stocks to comfortable levels. Consequently, domestic prices rallied in the 2H of the season to record levels of €1100-1200/mt, even higher than what was seen during the quota period. In turn, the higher prices attracted as much preferential and world market sugars that the EU market could find.

However, lack of availability from these traditional origins kept imports within the recent range of 2.2-2.3mmt. As expected in a deficit market, export parity remained closed, and quantities leaving EU(28) remained at the low levels of 0.9mmt for the second year running. The high price environment can be explained not just by low stocks as we go into the 2022/23 season, but also due to likely another poor crop output this year. Back in the spring of 2022, planting area reduced for a fifth consecutive season, this time dropping by 4.4%. Not only this, but another summer drought led to yields disappointing across the main producing countries (again). Production may come down 1.5mmt year on year. With preferential sugar availability dropping each year, where can Europe source to fill this deficit? The answer has come in the recently forgotten CXL raw quotas, which are likely to be close to fully utilised. The final curveball on imports will be how much sugar enters from Ukraine. Planting decisions are also being made for the 2023/24 campaign, with market consensus showing flat to a small increase.

- **CIS:** Putin's war in Ukraine undoubtedly has had a huge effect on the entire world and commodity prices in general, with sugar being no exception. Originally the move into Ukrainian territory was expected to impact production negatively, but that doesn't seem to be the case as expected production is close to 1.3mmt. With conflict in the east, exports to the CIS region were blocked off entirely. However, in its support for Ukraine, the EU granted duty free and quota free access for Ukrainian goods. As a result, by the end of November, Ukraine has exported 120kmt, well above their previous annual quota of 20kmt. Russia on the other hand is likely to produce 6.3mmt and export their surplus to CIS region. For 2023, the question remains how much of Ukraine's sugar will be exported to EU. The quota free arrangement is currently due to expire in June 2023, but it is very likely to be extended for another year, especially if the conflict is still ongoing. Planting in the spring is expected to increase by 20% as farmers and producers take advantage of high price environment in Europe. We could expect an even higher export availability next year. The 'stans' will likely be filling their domestic consumption once more with raw sugars from Brazil.

Macro

2022 will be remembered as one of the most volatile ones for macro, with trillions of dollars wiped off world stocks, bond market tantrums, whip-sawing currency and commodities and the collapse of a few crypto empires. The main drivers have been the war in Ukraine, combined with rampant inflation as global economies broke out of the pandemic, while China remained shackled by it. The drama kicked in as soon as the year kicked off, as it became clear that COVID was not going to shutter the global economy again and the world's most influential central bank, the U.S. Federal Reserve, was serious about raising interest rates. Ten-year Treasury yields have jumped to nearly 4% from less than 1.5% at the start of the year. Stocks are down almost 20%, while crude oil ends the year 8% higher, having been up nearly 80% back in early March. The Fed has delivered an eye-watering 400bps of rate hikes and the European Central Bank, a record 250bps, despite saying this time last year it was unlikely to budge.

The dollar reigned supreme throughout 2022, rising over 8% against the main world currencies; although at its peak, it was up nearly 20%, reaching 20-year highs as risk aversion and rising US interest rates led to a surge in demand. Initially, commodities rallied alongside the dollar (breaking the normally inverse relationship pattern). The war in Ukraine, coupled with a structural lack of supply-side investment caused energy, metals and agri commodities to soar. Indeed, the latter is set for the longest run of annual gains since at least the early 1990s as drought and war cut production and erode inventories, keeping global food inflation simmering. The Bloomberg Agriculture Spot Index is up 6%, the fourth straight yearly increase. However, the ongoing dollar strength, the continued lockdown of China's economy due to Covid and growing recessionary fears led to prices peaking in Q2 and by late Q3 had already returned to levels before the February invasion. Crude oil prices are back below $80/bbl, while natural gas has also plummeted (albeit still multiples of pre-Covid prices).

Looking ahead to 2023, it's doubtful whether commodity prices will continue to fall at the same pace. According to Goldman Sachs, commodities will remain the best performing asset class, with the S&P GSCI index returning 43% in 2023 due to insufficient capex to boost supply-side of (mostly) energy and metal markets. The bank suggests that just as commodity markets were dominated by the dollar in 2022, they will be shaped by underinvestment in 2023. For agri commodities, another bullish driver will be the re-opening of China's economy which will boost demand, alongside still-expensive fertilisers and volatile weather. The latter pertains to us being in another La Niña, which, being the third in a row, can cause all kinds of havoc to weather around the world. Perhaps even more worryingly, at some point in H2 of the new year, there's a chance we move into El Niño. And that really can lead to turbulent climate.

It is also our belief that the US dollar is unlikely to weaken much more from current levels. Most economists believe that the worst is yet to come, as the impact from hawkish monetary policy – designed to tackle rampant inflation - halts the post-pandemic recovery in its track. With the macro outlook for 2023 so negative, we may see a flight to safety, in which case the USD would benefit. If the dollar is to stabilise at current levels, then it follows that the recovery in other currencies may stop too. As such the euro may remain at 1.05-1.08 levels. The BRL, on the other hand, has a chance to strengthen. Having been crowned the best performing currency for most of 2022, a lot of the gains were wiped out after Lula's election win – even as other currencies started to rally as the dollar weakened. As such, there is much potential upside to be reaped from here on for Brazil's currency. So long as commodities continue to remain firm, and Lula's social spending plans do not blow the fiscal ceiling, there is a chance for the BRL to rally again to the low 5's. COPOM's early and aggressive rate hiking path of the Selic is taking effect, allowing inflation to cool in Brazil. This should provide a better environment for investors seeking carry trade opportunities.

Figure 5: Asset performance in 2022

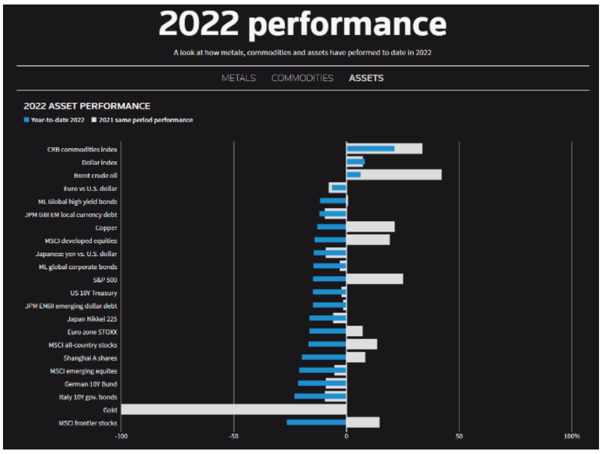
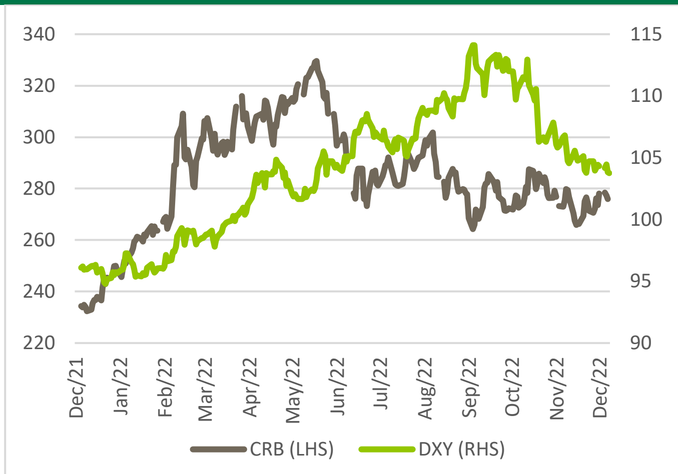


Figure 6: Commodity index v Dollar



Source: Bloomberg, ED&F Man Commodity Research

Wishing all our readers a very Happy New Year!!

Prices Table

New York #11					**London #5**				
(cents/lb)	19-Dec	30-Sep	% change		*($/tonne)*	19-Dec	30-Sep	% change	
Mar (23)	20.14	17.68	13.9%	↑	Mar(23)	553.2	492.0	12.4%	↑
May (23)	18.93	16.94	11.7%	↑	May (23)	535.7	481.0	11.4%	↑
New York #16					**White Premium**				
(cents/lb)	19-Dec	30-Sep	% change		*($/tonne)*	19-Dec	30-Sep	% change	
Mar (23)	36.16	34.94	3.5%	↑	Mar/Mar	109.2	102.2	6.8%	↑
May (23)	36.26	35.01	3.6%	↑	May/Mar	91.7	91.2	0.5%	↑
Macro					**Currencies**				
Indicators	19-Dec	30-Sep	% change		*Against US$*	19-Dec	30-Sep	% change	
CRB	270.6	268.3	0.8%	↑	Euro (EU) *	1.061	0.980	8.2%	↑
Gold	1,787	1,660	7.7%	↑	Pound (GB) *	1.215	1.116	8.8%	↑
Brent Oil	79.80	87.96	-9%	↓	Real (Brazil)	5.293	5.415	2.3%	↑
Baltic Dry	1,548	1,760	-12%	↓	Rupee (India)	82.65	81.51	-1.4%	↓
Handysize	701	1009	-31%	↓	Rouble (Russia)	66.00	59.20	-11.5%	↓
					(* rate is US dollars per FX)				