Research

Monthly Sugar Note

31 July 2023

Markets

The macro environment was more supportive in July as the latest economic data from the US showed lower than expected inflation numbers. US inflation figures in June saw CPI rising just 3.0%, below market expectations of 3.1%. After two years, it is finally getting closer to the Fed's target of 2%. The reduction in inflation has the market changing its opinion somewhat on how aggressive the Fed needs to be with its rate hikes. As a result, the USD index fell to 15-month lows, allowing commodities, equities and EM currencies all to rally.

The sugar market this month was supported by the more upbeat macro, but also by weather developments. In India, the monsoons came about 20 days later than normal, but have now reached similar volumes of rain to last year. While this may have added pressure to prices in the past weeks, the devil is in the details. The northern portion of the country may have received heavy rains above historical levels, but the southern portion saw several dry days. As a result, in Uttar Pradesh (representing about 30% of total sugar output in 21/22), cane development should be better than in Maharashtra (39%) and Karnataka (18%). Attention should also be given to the following crop (24/25) in the southern states as producers there may opt to cut the area to cane given the scanty rains.

Figure 1: C/S sugar production evolution

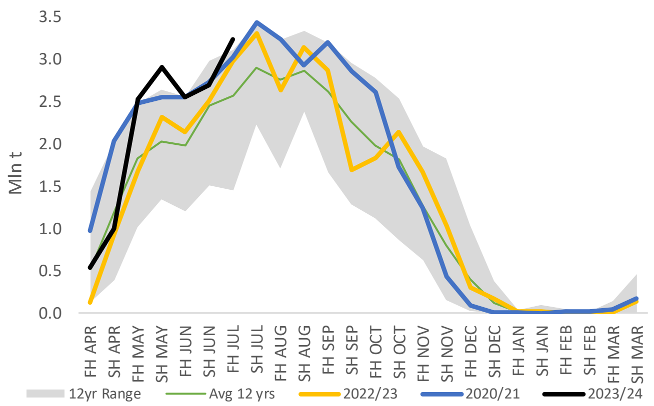
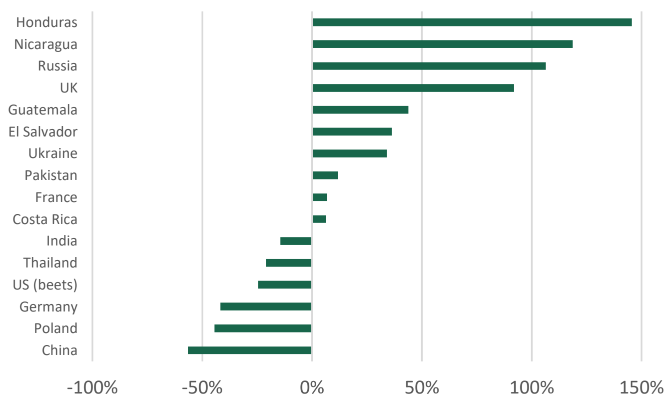


Figure 2: Rainfall var. 2023 vs. historical (01/07 – 20/07)



Source: UNICA and ED&F Man Commodity Research

In Brazil, benign weather has allowed the C/S crop to develop better than anticipated. Some analysts are now projecting sugar output close to 39mmt given the high agricultural yields the crop has been achieving, 19.5% higher YoY (in June) according to CTC. Up to mid-July, C/S crushed almost 260mmt of cane, 10.0% higher YoY with a sugar output of 15.5mmt, 2.8mmt ahead of the previous crop. The high sugar prices compared to ethanol has led to a few mills investing in sugar crystallization capacity for the next season. Every 1% of additional sugar mix results in about 700kt more sugar to the C/S production.

In the short term the market is paying attention to the excellent Brazilian crop, which is about 40% complete. It is also seeing shipments of C/S sugar to the world market flowing without much logistical issues. As a result, cash values are now trading at -20 points. If things stay unchanged, then it's reasonable to assume that NY11 will struggle to pass the 25c/lb barrier and may even test 21c/lb.

Longer term, however, we are starting to become pessimistic on the next Indian crop, while Thailand will at the very least have lower sugar output than 2023. For this reason, we project a deficit market for the next season and expect prices to stay firm.

The NY11 July contract ended with 412kt delivered from two tradehouses to three receivers. All the sugar was from Brazil. The July expired at 22.89 c/lb, while the Jul/Oct spread recovered from a discount earlier in the week to end at +10 pts. The August refined sugar contract expired in mid-July with a small delivery of 124kt delivered from India and Brazil. The August contract ended at $700.7/tonne with the Aug/Oct spread at $15/tonne.

Fundamentals

- **Brazil CS:** After the drop in cane quality observed in the Second Half of June, July's crop progress figures showed a vast improvement in cane quality and crushing. This ended any budding concerns over the 23/24 crop and gave fresh support to analysts in raising their sugar output forecasts up to 40mmt. Up to mid-July, C/S crushed 258mmt of cane, 10% higher than the same time of the past year. ATR value was 130.6kg/tonne, marginally higher than the past crop (130.5kg/t). With a sugar mix of 48.1%, sugar production reached 15.5mmt, 2.7mmt ahead of the past crop. Two things need to be considered for rest the crop. The first is the volume of cane to be crushed in the rest of the season; although cane crush volume reached almost 260mmt, there is still a big volume of cane to be crushed during the rest of the season which means we should see mills crushing in November and December. The second is the weather; *El Niño* should bring rains during the rest of the season which may delay the crop and decrease ATR. Meanwhile, the Government is discussing whether to increase the ethanol blend in gasoline from 27% to 30%. However, given that sugar is paying much more than gasoline, any increase would result in lower hydrous production without impact the sugar volume.

- **India:** The rainfall distribution in key sugar-producing states of central west India (Maharashtra and Karnataka) received below normal rains of -39% and -27%, respectively by mid June, although they have since recovered. Importantly though, the lower pre-seasonal showers and prolonged dryness during 1st June to 15th July has already negatively impacted crop growth. The crop condition is very poor in Maharashtra and Karnataka due to delayed rains and continuous dryness. The recent Indian Meteorological data shows near-normal rains across India, but a closer look sees the major cane region of central west India still in deficit. This is a worrisome situation for standing cane and new plantings for the 24/25 season. We believe that the negative impact that has already taken place on cane growth is not recoverable. Assuming a lower production estimate, India will not be able to export any raw sugar to the World Market. At the same time, raw sugar imports will have to increase to attend stand-alone refineries, as feedstock availability from the local market will be limited. Dry conditions should also affect the planting of the cane, reducing the production in the 24/25 crop.

- **Asia:** The dryness and above normal temperature story continues in Thailand, together with an uneven distribution of precipitation. The Central region saw a recovery in rainfall in the last 30 days, but the major area of the Northeast is still dry, with 40% lower rainfall YoY since July. Our 23/24 crop estimate for Thailand is now towards the lower end of market range of 70-80mmt, with more downside if rainfall shortage persists. Looking into the current crop, we see decent whites demand giving certain support to Thai cash premium. Thailand EPZ is essentially consuming the stock available for traditional export business. Besides, Philippines has shown good appetite for sugar and is importing another 150k to address high domestic price. By contrast, sugar demand is sluggish in China due to high prices and increasing competition from alternative sweeteners. That said, Brazil line-ups to Asia started to pick up this month and we should see at least 1.5mmt China demand in Q3'23 to complete imports via quota.

- **Centrals:** The 2022/23 season has finished with combined production for Centrals at 5.1mmt, around 5% lower than the year before. The focus is now on the rains, as despite some improvement in the past weeks, the beginning of the development period saw less than ideal rainfall. This could be an important risk, as the Centrals already saw a reduction in output this year. As such we could see the regional market that is highly dependent on Centrals' sugars, face another year of tightness.

- **EU/UK:** The EU commission published their estimates for the EU(27) countries for the 22/23 crop year at 14.6 mmt, 12% lower than 21/22. For 23/24, The EU Commission forecasts 15.5 mmt of sugar, up 6% from their 22/23 estimate. The beet area planted has increased as well to 1,378 kmt, up by 2.9% YoY. The latest MARS report showed EU beet yields projected at 73.3t/ha, 2% higher than the historical average. Despite this, soil moisture levels in parts of Northern Poland, Eastern France, and Western Germany have recorded drier than normal levels, due to lower rains and possibilities of drought conditions coming up. France has started showing signs of cercospora, with regions south and east of Paris, looking to start spraying insecticides to reduce risk. The UK on the other hand has had a good combination of dry weather and rain showers which has been conducive for the growth of beets. All in all, we see higher production in 23/24, but ending stocks will continue to be low, supporting high local prices.

- **CIS:** Russian sugar beet sowing area stands at 1.04 mmt for the 23/24 crop. The Russian beet test that was released on 11 July showed an average root weight of 173g, which is 29g higher y-o-y. This shows promising crop results for 23/24. Russia has decided to end the Black Sea Grain Deal after it expired on 18 July, as it wants to improve the exports of its own grains and fertilizers to the world. While this is supporting grains prices, it has less impact on sugar. Ukraine on the other hand, has a beet area of 241 kha, resulting in a crop 50-60k higher than 22/23. The weather in Ukraine has been suitable for the development of sugar beets and thus we expect Ukraine to have a good crop for 23/24. As such, it will continue to see massive exports of 45s from the region, mostly into the EU. Ukraine also eased the ban on sugar exports and has allowed exports of 20 kmt of sugar to Romania until September 15th, 2023.

Focus – Mexico and US

With both Mexico and the US in their intercrop period, the main concerns currently are related to weather and crop development, domestic prices and imports. As a new cycle of discussions on the regional trade flow approaches and given the poor performance of Mexican crop in 2022/23, the potential recovery on the fields will be key. This will determine how much sugar could potentially be the US quota for the new crop and have implications on other import mechanisms, such as TRQs and high duty imports.

From the Mexican perspective, the new crop should see an improvement YoY. The 2022/23 crop registered a drop of 16% in sugar production to only 5.23mmt, with irregular weather and high prices of fertilizers the main reasons behind the drop. With fertilizer prices softening from a year ago, treatment of cane is expected to improve. However, weather

behaviour is yet to be seen, as some regions are still facing dry weather and high temperatures. There are important rainy months ahead that could shift production in many ways. But depending on how the rainfall goes, the projected number from the USDA, of 5.9mmt, can change. In any case, around 1.3mmt of sugar could be exported in the new season which means that Mexico will stay away from the World Market again, and export only to the US.

With poor production, Mexico's SnD became extremely tight this season, and the country has been seeing near continuous rises in domestic prices. This reduced the IMMEX intake and triggered massive volumes of imports. Even their 2022/23 export quota to the US will probably not be fulfilled, as the low pol raws production fell short of the quota. Meanwhile, domestic sales up to June were still showing good levels compared to the year before. This tightness should remain at least until the beginning of the new campaign, so high prices and high flow of imports should be expected at least for the next four months.

From the US perspective, USDA expects a very similar crop YoY on a combination of 2% growth in cane sugar and an offsetting 2.4% reduction in beet sugar. Despite a reduction in beet acreage, plantings were less delayed than last year, and fields rated as good or excellent are in general similar or better than the year before. With that in mind, it could be possible to see an increase in beet sugar volumes adding to US SnD. Still, the feeling of tightness can still be seen in the country and imports will likely continue at a high pace - especially high duty imports, oversubscribed Specialty quota tranches, and more recently an increase on raw TRQ volumes. Even for the new crop, USDA has already increased its estimate of refined high duty imports, acknowledging that the mechanisms will likely continue.

Figure 3: Sugar production

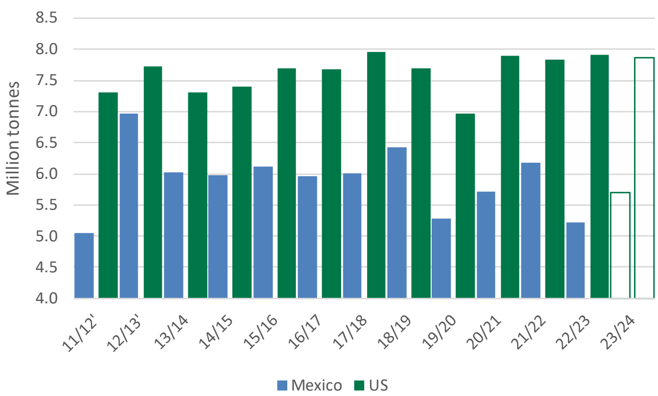
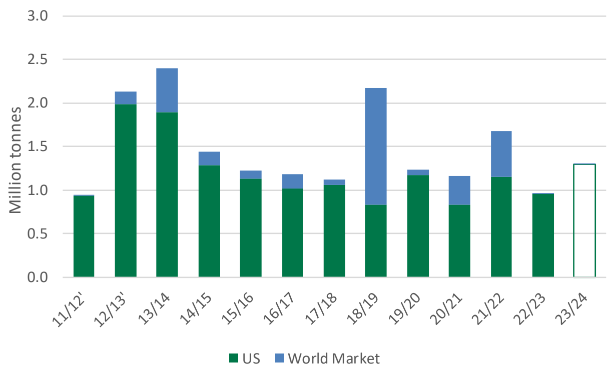


Figure 4: Mexico sugar exports per market



Source: Conadesuca, USDA and ED&F Man Commodity Research

Certainly, many moving pieces remains for both countries' SnD and trade flows. At this pace the projected new crop quota for Mexico should reduce from its current estimate, but it doesn't mean Mexico will have significant World Market volumes either, as its crop is also likely to be revised down. On the other hand, it could be another year with room for other import mechanisms to play important roles, mainly TRQs and high duty imports, which are likely linked to regional origins of sugar. If so, this would keep the whole Americas region in a tight scenario once again.

Macro

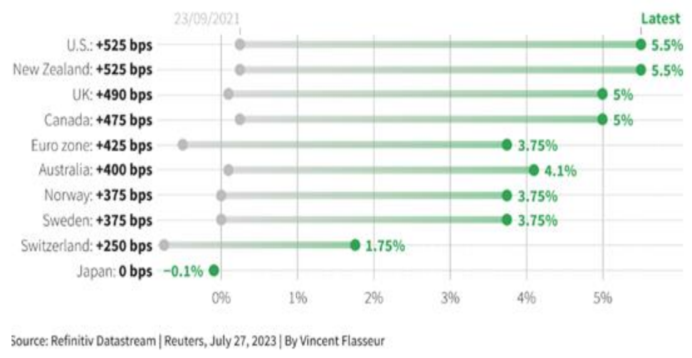
Risk-on moves, fuelled by growing expectations that central banks are nearing the end of policy tightening campaigns, are boosting the outlook for global growth and energy demand. Inflation is easing in most countries, but they remain high, with divergences across economies and inflation measures. Following rising gas inventories in Europe and weaker-than-expected demand in China, energy and food prices dropped substantially from their post-Ukrainian invasion 2022 peaks in H2 2023. Together with the normalization of supply chains, these developments contributed to a rapid decline in headline inflation in most countries. Core inflation, however, has on average declined more gradually and remains well above most central banks' targets. In response the Federal Reserve, after having paused rate hikes at its June meeting, hiked again last week. The European Central Bank followed suit, as did other central banks, with the notable exception of Japan and China, where slowing economic trends are, if anything, giving reason for monetary stimulation.

According to the IMF's latest outlook, global growth is projected to fall from a 3.5% in 2022 to 3% in both 2023 and 2024. They expect the rise in central bank policy rates to continue to weigh on economic activity. Global headline inflation is expected to fall from 8.7% in 2022 to 6.8% in 2023 and 5.2% in 2024. Still, the month of July saw a more upbeat macro environment, with commodities in particular making a strong recovery after the lacklustre first half of the year. The US economy grew faster than expected at 2.4% annualised in Q2 as a resilient labour market supported consumer spending, while businesses boosted investment in equipment and built more factories, potentially keeping a much-feared recession at bay. This is leading markets to price in a "soft-landing" scenario, which in turn is causing markets (notably equities) to soar.

Oil prices are on track for a fifth straight week of gains with investors optimistic healthy demand and supply cuts will keep prices buoyant. The rally is due to the OPEC+ cutbacks, which has led to a tighter global supply/demand scenario for H2 2023. Agricultural commodities also got a lift, following the advent of El Nino and record temperatures around the world, as well as Russia coming out of the Black Sea grains corridor. The threat of reduced supplies out of Ukraine led to higher grains prices, made worse by India banning non-basmati rice exports and drier weather in the US corn belt. Even metals, the underperformer within the commodities complex, managed to stage a recovery, on hopes that China would stimulate its way out of the erstwhile sluggish demand for raw materials.

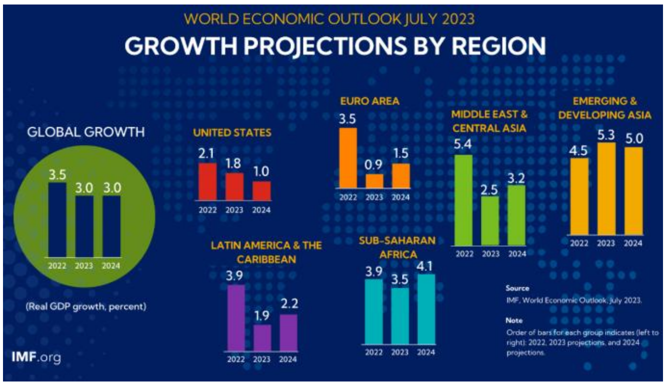
Brazil's central bank is poised for its first interest rate cut of 25 bps next week, the first in 3 years. After pushing the benchmark rate 1,175 bps higher to combat pandemic-driven inflation and shocks in energy and food prices, policymakers have held at 13.75% since September 2022, drawing rebukes from President Lula da Silva. Consumer inflation in the 12 months to mid-July slowed to 3.19%, dipping below the central bank's official target of 3.25% for this year. Still, carry trade opportunities continue to favour the BRL, which at 4.72, remains one of the star EM performers this year.

Figure 7: Central bank hikes



Source: Reuters, ED&F Man Commodity Research

Figure 8: IMF's latest forecasts



Source: IMF, ED&F Man Commodity Research

Upcoming Areas of Interest

- **Brazil C/S –** Can the strong crop progress continue?
- **Brazil C/S –** Ports efficiency given strong grains exports
- **India –** Monsoon development
- **El Niño –** Implications on Brazilian and Asian crops

Prices Tab

New York #11					London #5				
(cents/lb)	27-Jul	30-Jun	% change		*($/tonne)*	27-Jul	30-Jun	% change	
Oct (23)	24.43	22.79	7.2%	↑	Oct (23)	686.5	628.2	9.3%	↑
Mar (24)	24.64	22.89	7.6%	↑	Dec (23)	678.4	627.3	8.1%	↑
New York #16					**White Premium**				
(cents/lb)	27-Jul	30-Jun	% change		*($/tonne)*	27-Jul	30-Jun	% change	
Sep (23)	38.29	39.00	-1.8%	↓	Oct/Oct	147.9	125.8	17.6%	↑
Nov (23)	39.95	39.51	1.1%	↑	Dec/Oct	139.8	124.9	12.0%	↑
Macro					**Currencies**				
Indicators	27-Jul	30-Jun	% change		*Against US$*	27-Jul	30-Jun	% change	
CRB	280.2	262.0	6.9%	↑	Euro (EU) *	1.097	1.091	0.6%	↑
Gold	1,945	1,920	1.3%	↑	Pound (GB) *	1.279	1.270	0.7%	↑
Brent Oil	84.24	74.90	12%	↑	Real (Brazil)	4.742	4.786	0.9%	↑
Baltic Dry	1,097	1,091	1%	↑	Rupee (India)	82.15	82.09	-0.1%	↓
Handysize	397	446	-11%	↓	Rouble (Russia)	90.70	86.95	-4.3%	↓
					(* rate is US dollars per FX)				