Research

Monthly Sugar Note

30 August 2023

Markets

The July rally that we saw across the commodities complex faltered in the first half of August. In part this was due to a stronger dollar, as the US economy continues to show signs of resilience despite 525 bps of rate hikes since March 22. This is prompting the US Fed to maintain a cautionary yet hawkish tone even as inflation eases. Another factor was the negative economic data coming out of China. Weak property growth and poor trade figures, together with high unemployment, especially among young people, is a bad sign for the commodities market.

Sugar was little impacted by this negative macro scenario, however, as it continued to trade within a 23-25 c/lb range. In the short term, the market continues to rely on the good progress of the C/S Brazil crop. Up to mid-August, C/S crushed 360mmt of cane, about 12% higher YoY, with sugar output at 22.7mmt, 4mmt ahead of the previous season. August numbers should continue to show large figures as El Niño is still not bringing in wet conditions in the C/S cane belt, despite a few showers in the last week of the month. World Market demand has been strong for this sugar, but the good crop figures – along with the lack of logistical issues impacting the flow of exports to date – has allowed cash values to drop significantly, trading at -40 points at the moment.

Petrobras announced a gasoline price hike of 16.2% and a diesel increase of 26% in August. However, hydrous ethanol on a sugar equivalent basis is estimated close to 15.5c/lb, meaning it poses little threat to the sugar mix. All in all, assuming Brazil will be able to reach a sugar output of over 39mmt (vs. 33.7mmt in 22/23), NY11 may find it difficult to sustain prices above 24-25c/lb in the short term.

Figure 1: 2023 rainfall changes with LTA (as of Aug 28th)

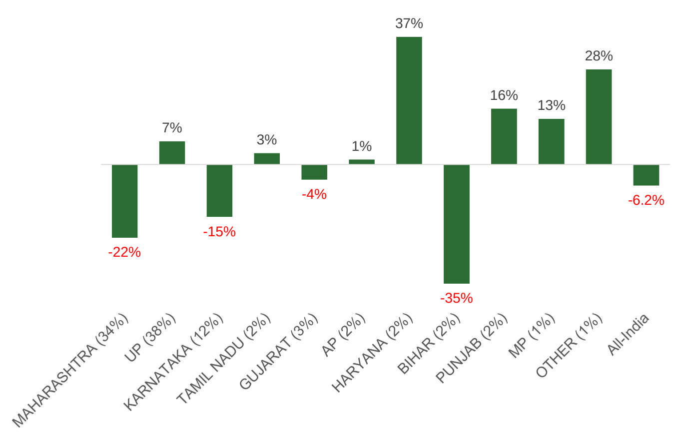
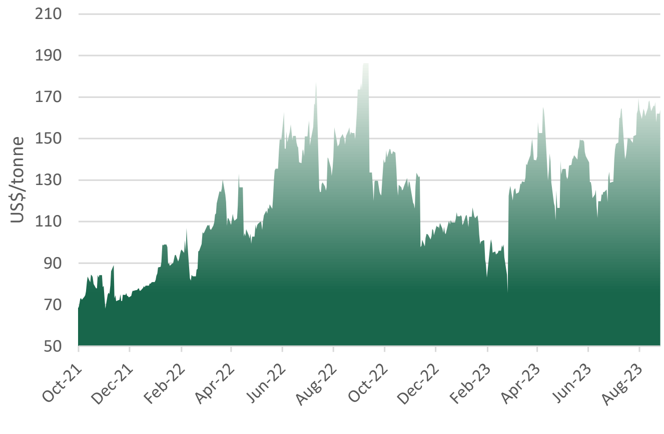


Figure 2: White Premium (front month)



Source: ED&F Man Commodity Research

The medium-term outlook, however, is turning more bullish. The current market mood is unlikely to continue once the 23/24 (Oct/Sep) season commences, given the unfavourable weather in India and Thailand. The late Indian monsoon improved slightly in July, but August figures are indicating an early end to the rains. This will reduce the potential growth of the next crop, as well as planting for the following season (24/25). With this in mind, the Indian government has started to indicate that it may ban sugar exports in the next season (something we have been expecting for a while now). This news allowed prices to move out of its recent trading range, surpassing 25c/lb level in the last days of August.

Without Indian sales, and given our lower Thailand crop projection, the deficit in the 23/24 season will need a solution. This means that prices will have to move higher in order to cut demand. To note, weather permitting, we expect Brazil to increase output in 2024 too, as crystallization investments are already being noted in the country. However, local ports may struggle to surpass current monthly exports volumes due to insufficient port capacity.

With the end of the Indian exports, the supply of refined sugar has decreased considerably in the past months, taking the White Premium close to $170/tonne, indicating that stand alone refineries are needed to rescue the market. Indeed, refineries in India, Saudi Arabia and Morocco have understood the message as we can observe their presence in the Brazilian line ups. But some refineries, like in UAE, Algeria and Tunisia, are struggling to reach their maximum capacity, which is helping support the White Premium. We expect the whites market to ease off as soon as the Northern Hemisphere crops start. However, similar to the raws market, 2024 is also in need of whites supply. As such a high White Premium may remain a feature in the new year too.

Fundamentals

- **India:** The rainfall distribution in key sugar-producing states of central west India (Maharashtra, Karnataka, and southern states of India) which contribute around 60% share of India's production, have all received below-normal rains. The Maharashtra rainfall weighted by cane areas is 20% below average and Karnataka is -14% as of 23rd August 23. With this continuous dry weather pattern and, looking at the short-term forecast, we may see further negative impact on agricultural yields. The Maharashtra cane commissioner's office held a meeting with the agri officials of various sugar mills and their initial Maharashtra crop estimate for the 23/24 season is 1mmt lower than the 22/23 season. Also, so far, the main reservoirs that serve the water for irrigation in the main sugar-producing states of Maharashtra & Karnataka are down by 40% and 25% respectively, compared with the same time last year. If no improvement in reservoir levels are seen in September, we could see a big risk to 24/25 production. Given the lower production forecasts, we expect tight domestic availability & higher prices despite higher monthly sales quota releases. Currently, the domestic market is trading around 35500 to 36000 INR/MT.

- **Asia:** Rainfall in Thailand continues to be disappointing, particularly in the North and Central regions. Despite good rainfall in the key North-East area in July, August has so far been lacklustre. This dryness is consistent with a poor cane crop of around 70-80mmt. The Sugar Mill Association and Sugar Cane Farmer Association's second crop estimate for 23/24 was recently published at the 82.4-86.6mmt cane range. This is an -11% drop from their first estimate back in May. Nevertheless, we believe there may be further downside to the cane number due to persistent dryness. On the demand front, the high flat price and weak economic conditions in China has been impacting consumption and demand estimates. Buying across other regional destinations remain hand-to-mouth, although depletion of domestic stocks may mean that domestic prices have to rally first to bring import margins back to positive territory.

- **US:** The August WASDE report had several updates for the US market. In the 2022/23 crop, there was a minor reduction of 10k MTRV in US beet sugar production, while imports were raised by 144k MTRV. This increase is due to the rise of 68k MTRV in Re-exports (after a big cut in July). Additionally, imports of TR2 (full duty) rose by 36k MTRV, and Mexican imports were also up by 39k MTRV. Despite an already anticipated 23k MTRV reduction in food use, ending stocks went up by 157k MTRV, reaching a 15.8% stock-to-use level. Moving to the 2023/24 crop year, on top of higher beginning stocks, production only saw a marginal rise of 3k MTRV (46k higher on beet mostly offset by 43k lower on cane, particularly in Louisiana). Imports were up by 41k MTRV, driven by a 68k MTRV increase in Re-exports, in line with 22/23, and a 9k MTRV increase in TR2 estimates, however, TRQ imports were decreased by 36k MTRV due to an estimated shortfall in the recent additional TRQ. All in all, ending STU are at 15.2%. While exports are still unchanged (despite strong export activity to Mexico), the current STU level indicates a theoretical surplus of 200k MTRV in the US market, implying that without further adjustments to the SnD, USDA is likely to decrease the Mexican quota by this same amount. Currently 50% of the July Mexican quota is guaranteed (674k MTRV out of 1348k MTRV). As per the current suspension agreement, 70% of the volume published next month will then be guaranteed.

- **Mexico:** Mexican mills may be in their intercrop period, but the market has been very busy with large volumes of imports. Given production was 16% below the previous year, in the face of strong consumption, domestic prices have skyrocketed, incentivizing imports from all over the world. Sugar has arrived from India, Centrals and Brazil, and even from the US. The market is now following weather developments to see how much of a production recovery can be seen, but until July the producing regions were all seeing a rainfall deficit. August has had better conditions, especially on the Pacific side, but there is a significant delay in rains. Still, given better cane treatment, production is expected to see a recovery. But if weather in August doesn't finish with rains at or above average for all regions, Mexico's sugar output may stay at low 5mmt levels.

- **Centrals:** The 2022/23 crop finished with a combined production of 5.1mmt for all of the Centrals, around 5% lower YoY. Currently, attention is on the intercrop rainfalls. Although the initial months of cane development had below average rains, the situation has improved over the past few weeks, resulting in a more favourable outlook for the crop. This is particularly significant as Centrals had already faced a reduction in production at the 2022/23 season, adding to the regional market tightness. Still, the current improvement is still modest, leaving the crop somewhere between similar levels YoY to a small increase.

- **EU/UK:** The August MARS report showed improvement in yields across Europe. This can be attributed to the cooling of temps that took place in Europe in August after the drought/heat wave that rampaged the region. The dryness in northern & and north-western France, and Southern & and western Germany was alleviated by a rain surplus. The abundant rain during this period benefited summer crops in particular areas previously affected by rain deficit. Furthermore, MARS increased yields for France and Germany to 81 t/ha and 74.6 t/ha, respectively. The largest increases in yields were for Hungary and the Czech Republic with 67.2 t/ha. On the other hand, looking at the sugar content in the initial beet tests around Europe, we see that beets have been impacted by the late planting. However, with ideal weather conditions hence forth, things could change very quickly. For example, in Germany beet weights are already improving, and we expect beets to develop even more to show an increase in sugar content. This brings us to a production number above 15.5 mmt for the EU(27) and 1 mmt for the UK, with an upside flag in case beet tests start showing improved sugar contents and yields.

- **CIS:** Russia has begun the harvest of sugar beet, with Lipstek, Oryol, Tambov all starting beet harvesting two weeks earlier than average. About 4.4% of sugar beets in Russia have been harvested, amounting to roughly 2,242 kmt. Based on the latest sugar beet tests in Russia, we are looking at a very promising crop, with beet weights at 505g and top weights at 436g. However, the sugar content is at 14.2%, lower than in previous years. This takes us to a 23/24 production close to 6.4 mmt, and higher Russian exports. Alongside Russia, Ukraine is estimated to have a good crop with new planting figures at 249.9k ha (compared with the last number of 239.7k ha). Accounting for this jump in acreage, production can surpass 1.7 mmt, with Ukraine now able to export more than 600kt of sugar, most of which will make its way into the EU. In addition, 15 Sep will mark an end to the ban imposed by the Ukraine government on sugar exports, which would flush the market with more white sugar during the last month of the season.

Focus – Brazil C/S - A year of records… and not over yet

After an extremely poor crop in 2021/22, C/S Brazil saw a marked improved in the 2022/23 season, but the performance of 2023/24 is so far unprecedent. The combination of investments in the fields and an almost perfect weather pattern during all the important months should lead to an agricultural yield growth of around 25%, reaching levels of above 90t/ha, a projected record. Weather has also been helpful during the crush period, as it has been raining below average during the peak of harvest. This has allowed for a very fast paced crushing, resulting in other records - a monthly crush of 101.3mmt was registered in July (4mmt more than the previous record) and a record monthly sugar production of 6.9mmt (0.4mmt above the previous record).

Similar to July, crop results during the First Half (FH) of Aug were also strong. Millers crushed 47.8mmt of cane, 24% higher YoY, taking the total crush since the start of the season to 360mmt, 38mmt ahead the past crop. ATR reached 149kg/tonne (vs.153kg/t in 22/23) while sugar mix was at 50.1% (vs. 46.7% in 22/23). Sugar output reached 3.5mmt during the period (vs. 2.6mmt in 22/23). Since the start of the season, C/S Brazil's sugar output totalled 22.7mmt, 4mmt ahead of the previous crop.

Although the crush presents a good pace, there are concerns about the tail of the crop, as there is still a substantial volume of cane to yet be crushed. If rains return early - which is a possible outcome of El Niño in C/S - there may be lots of cane left uncut (bisada), an undesirable scenario. With the massive agricultural yields presented, cane availability would surpass 630mmt, but depending on the volume of leftover cane, crush could reach 610 – 620mmt.

Figure 3: Sugar production

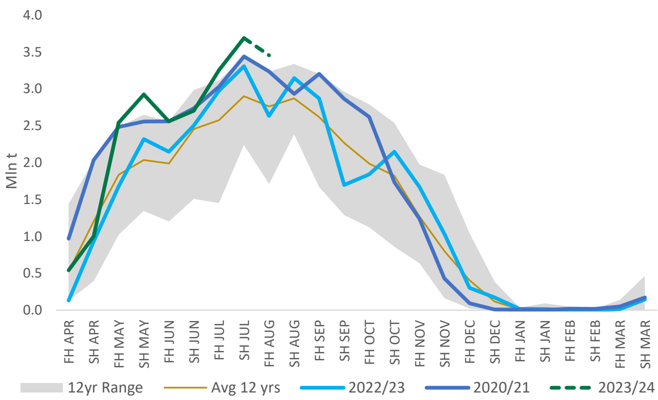
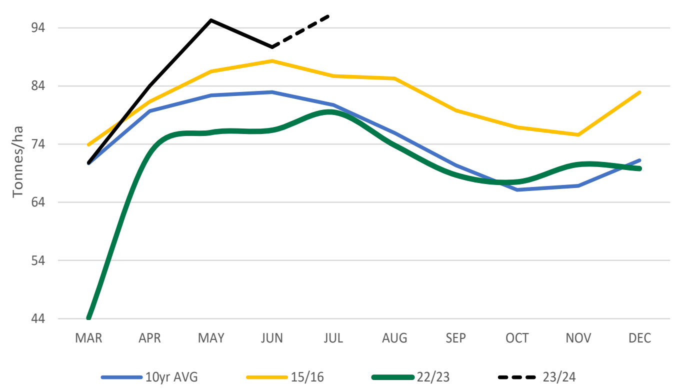


Figure 4: Agricultural yields evolution



Source: UNICA and ED&F Man Commodity Research

Despite the good total fuel demand registered in 2023, hydrous demand has only now started to pick up. But with current pump prices it should sustain for a few months before ethanol prices rise to the point of losing demand. Still, this rise should not be anywhere close to sugar prices, which should remain supported as there are supply concerns in other major producing countries ahead. With that, the sugar mix is also setting new records and should finish at almost 49%. This percentage could be even higher the following season thanks to several new investments in the mills. The combination of all these strong factors should lead to a 2023/24 sugar production of almost 40mmt for C/S Brazil, another record.

With this level of production and good exports demand, space at the sugar terminals has been challenging as there is fierce competition for space with the other massive crops Brazil has been reaping, namely soybeans and corn. Still, C/S should be able to export more than 30mmt over the course of the season. However, weather delays, as seen in late August, should be more frequent now, rolling volumes forward into another massive crop expected for next year. All in all, this crop could yield several records, both in the fields, the mills, and at the ports.

Macro

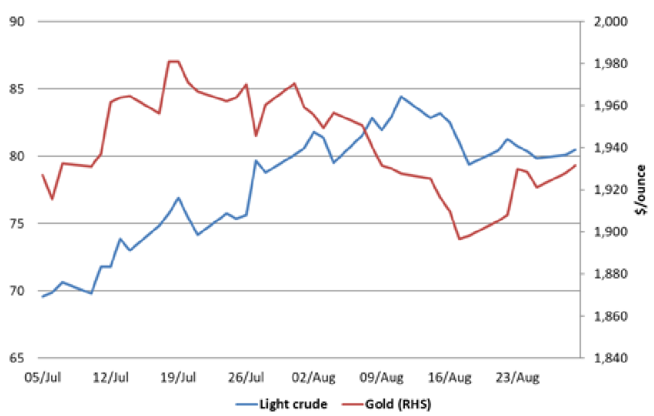
August proved to be a much less buoyant month for markets compared to July, with the US dollar strengthening steadily against other currencies, amidst rising US treasury yields and worse than expected data out of China. Markets had priced in peak Fed rates in July, but subsequent economic data out of the USA suggested a resilient economy that may warrant further rate hikes. At the Jackson Hole Symposium, the Fed chair reiterated the message that inflation was still running ahead of target and that the next moves would be highly data dependent. Perhaps reflecting this sentiment, the month saw a strong sell-off in US treasuries, with 10-year US yields are almost back at 4.25%, 16-year highs. The sell off in bonds is the market reminding us that inflation pressures are still not gone, and that rates will need to stay higher for longer.

Across the rest of the world, PMI data have been coming in weaker than expected, suggesting the economy is slowing in Europe and China. Indeed, the euro has weakened versus the dollar in anticipation of the ECB pausing its planned September rate hikes German business activity contracted at the fastest pace in over three years in August and much more than analysts expected. Similar trends were seen elsewhere in the Eurozone and UK. Crossing over to Emerging markets, we saw better performance in Brazil, where new tax reforms are being approved by congress, just as inflation comes in line with target. The improving economic fundamentals are attracting investor flows into the BRL, which already is benefitting from carry-trade opportunities.

Figure 7: US Govt bonds reach 16yr highs

Source: Reuters, ED&F Man Commodity Research

Figure 8: Crude oil may have peaked out



Source: Bloomberg, ED&F Man Commodity Research

One economy that is causing concern to the world of commodities, however, is China. The second half of August saw markets trading risk-off on the back of growing signs that China's economy was slowing. The country is actually suffering from deflationary pressures, with both trade volumes and fixed asset investments falling sharply. Fixing the China problem is not going to be an easy task, and piecemeal attempts to stimulate the economy by reducing

interest rates here and there are clearly either too little or not effective enough. China needs to fix its structural issue of low household consumption and move away from state-led infrastructure investment and export led growth (the latter increasingly important as the West shifts away from trading with China).

The China drag, along with a stronger US dollar, is not a favourable backdrop for commodities. There is a chance that the highs may have been made for the year in crude oil, at $85/bbl, if demand (led by China) starts to weaken. Metals are also struggling for similar reasons, while grains - which had earlier received some support from the Black Sea geopolitical issues and US weather markets – are now falling amidst harvest pressure.

Upcoming Areas of Interest

- **Brazil C/S –** Crop progress and port capacity
- **Brazil C/S –** Start of the rainy period and disruptions to crush
- **India –** Monsoon development and cane yield impact
- **India –** Government announcements regarding the next sugar crop
- **El Nino –** Implications on Brazil's and Asia's crops

Prices Tab

New York #11					**London #5**				
(cents/lb)	29-Aug	31-Jul	% change		*($/tonne)*	29-Aug	31-Jul	% change	
Oct (23)	25.45	24.11	5.6%	↑	Oct (23)	724.9	683.3	6.1%	↑
Mar (24)	25.76	24.29	6.1%	↑	Dec (23)	713.4	673.0	6.0%	↑
New York #16					**White Premium**				
(cents/lb)	29-Aug	31-Jul	% change		*($/tonne)*	29-Aug	31-Jul	% change	
Nov (23)	41.50	40.85	1.6%	↑	Oct/Oct	163.8	151.8	7.9%	↑
Jan (24)	41.71	41.75	-0.1%	↓	Dec/Oct	152.3	141.5	7.7%	↑
Macro					**Currencies**				
Indicators	29-Aug	31-Jul	% change		*Against US$*	29-Aug	31-Jul	% change	
CRB	279.8	282.2	-0.8%	↓	Euro (EU) *	1.088	1.099	-1.1%	↓
Gold	1,937	1,964	-1.4%	↓	Pound (GB) *	1.264	1.284	-1.6%	↓
Brent Oil	85.49	85.56	0%	↓	Real (Brazil)	4.852	4.724	-2.7%	↓
Baltic Dry	1,107	1,127	-2%	↓	Rupee (India)	82.57	82.24	-0.4%	↓
Handysize	514	394	30%	↑	Rouble (Russia)	95.42	91.75	-4.0%	↓
					(* rate is US dollars per FX)				