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Sugar: Just taking a breather

Having absorbed the bullish Indian output picture, sugar prices have slipped into a one-month-long consolidation (Chart 1). Where to from here?

Brazil

The bearish overhang is Brazil. The key to the future of sugar prices is knowing what the ethanol/sugar production ratio will be for the 2023-24 crushing season that began in March. Analysts persist with forecasts that 48% of cane will be crushed into sugar, the highest ratio in many years. Mills report bi-monthly, and thus far, the ratio has been 38%, but it's much too early to judge. Production in April was actually below analysts' expectations because heavy rains hampered harvesting. The forecast going forward is mixed, with the presence of El Niño being cited as a potential for heavier-than-normal rain. While this should not affect the ethanol/sugar ratio, it could mean that total available cane estimates are a tad too exuberant.

To quantify the widening gap between sugar and ethanol prices, consider that the sugar-price equivalent of the spread between sugar and ethanol is currently being quoted at about 11¢ per pound. That is the widest spread since 2011. By the same token, there is a cap on how much cane mills can divert to sugar, because domestic ethanol demand does not have too much elasticity on account of the minimum, government-required blend in all vehicles.

One bullish factor that has emerged on the Brazilian front is that the ports are clogged with grain shipments. The maximum monthly capacity for sugar at the moment is 2.8 million tonnes, which is below last year. With record soybean and corn crops coming to market, this is not a problem that will dissolve easily, as all these crops compete for space at the docks. One analyst says that it will take 10 months to clear the backlog enough to allow sugar exports to return to normal levels.

India

There has not been any fresh news out of India. What we know is that they have shipped 5.7 million tonnes in the marketing year 2022-23, with export licenses capped at 6.1 million tonnes. So not much more coming out of India. That's far below last season's 11 million tonnes, and as it turns out, more than they should have sold in terms of assuring the availability of sufficient domestic inventories.

As far as total output is concerned, the estimates are still at between 32 and 33 million tonnes, down from 36 million tonnes in 2021-22. That estimate has been around for about two months now. Based on the early shuttering of mills, we consider it a high probability that the next time we see a production estimate update, it will be lower.

On May 22, the International Sugar Organization revised its estimate for the 2022-23 global production/consumption surplus to 850,000 tonnes, down from 4.15 million tonnes in its February estimate. We believe that this forecast is subject to revision as well, once we see where Indian output is really at.

We are long July 20¢ calls, first recommended on January 29 when they were trading at about 60 ticks. Those calls are now trading at about 5.50. With the options expiring in mid-June, we suggest accepting the handsome profit and rolling into October 27¢ calls, currently trading at about 1.30.

[By Sholom Sanik, May 25, 2023]

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Chart 1 – ICE July sugar

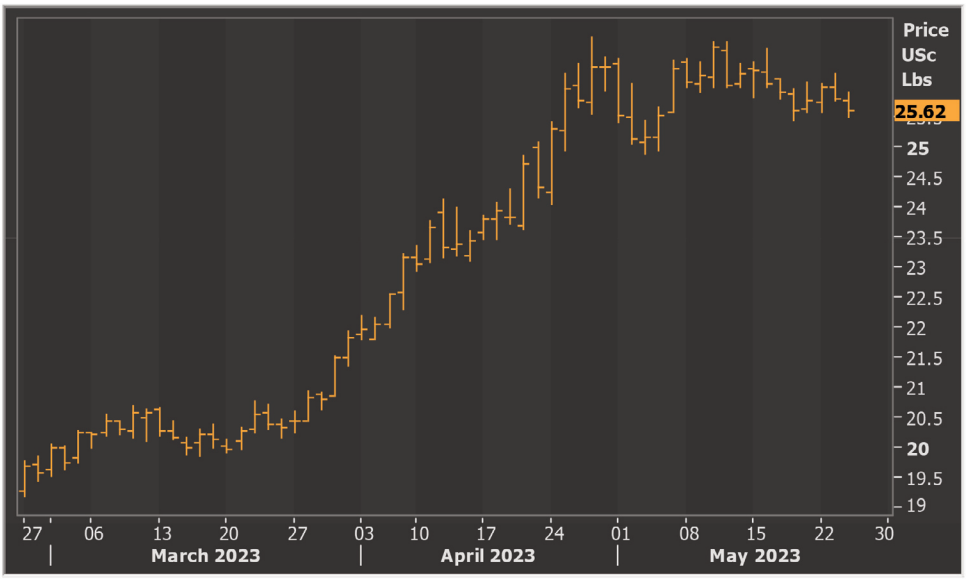


Chart courtesy Reuters

SOYBEANS

Weather and China will rule

Soybean prices have fallen by more than $2 per bushel since mid-April. The primary bearish factor has been planting progress of the US 2023-24 crop. As of the most recent weekly progress report, 83% of the crop has been planted. That compares with 64% at this time last year and a five-year average of 65%. Certainly, when viewed in isolation, that is a staggering achievement. It translates into an early harvest and just about eliminates any exposure to frost risk at the tail end of the harvest period.

The first comprehensive look at the 2023-24 crop year was presented in the May USDA crop report. Yield was estimated at 52 bushels-per-acre (bpa). That would tie the record set in 2016-17. If accurate, that would be up sharply from last season's poor performance of 49.7 bpa. We believe that the bearish exuberance associated with getting the crop in early is a bit premature because the weather has been dry in the corn belt and the forecast calls for more dry weather, at least in the near future. Rain is needed. The yield estimate is based on excellent weather, but rain in May and the first part of June is crucial. Historically, early friendly yield estimates will fall by about 3% without adequate May and June precipitation.

The USDA increased 2022-23 Brazilian output again in the May crop report, by 1 million tonnes, to 155 million tonnes. Looking at South America as a whole, that was not terribly bearish because of Argentina's crop failure. Production is estimated at 27 million tonnes, down from 43.9 million tonnes in 2021-22. Either way, at this point South America is neutral because, for the most part, these estimates have been known for several months.

Turning to the demand side, US export sales have contributed to the bearish sentiment. The USDA estimate for 2022-23 sales is 54.84 million tonnes. With three months remaining in the marketing year – in a word – we're not going to make it.

Commitments stand at 50.8 million tonnes. New sales have been dwindling, and with Brazilian supplies becoming available, it is near impossible to reach the USDA target. Besides, shipments have been lame as well. Last year at this time we were averaging about 500,000 tonnes per week. Over the past three weeks, shipments have averaged about 200,000 tonnes. In April, the USDA actually raised its estimate for annual US exports by 600,000 tonnes and stuck with it in May. Once the USDA incorporates onto its balance sheet the reality that foreign sales for the current marketing year have dried up, we will see a meaningful uptick in 2022-23 carryover stocks.

Looking ahead to demand for the 2023-24 crop that is now growing, it doesn't get much brighter. Last year at this time US exporters had contracted to sell 11.8 million tonnes of new-crop beans. That figure for the 2023-24 marketing year stands at a paltry 2.5 million tonnes.

Going forward, we believe that prices will be driven by

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US weather. After all, the market has priced in perfect weather. Just a whiff of dry weather has popped the market by 60¢ off the recent low. On the other hand, demand for US beans has waned. That is certainly true for the short term.

Having said that, China is always a wild card. Chinese production continues to provide only a fraction of their requirements. According to the May USDA crop report, this coming season will be no different. Production is stagnant at just over 20 million tonnes, while consumption is forecast to rise by 6 million tonnes, to 118 million tonnes.

So soybean imports remain a way of life for the Chinese. If there is a resurgence of Chinese demand coupled with a less-than-perfect US crop, what we've seen in recent days may very well have been the bottom of this market.

On April 5 we suggested establishing long positions in July soybeans at $14.80 per bushel, mercifully, with a stop at $14.20, which has long been triggered. We will stand aside while monitoring developments in the US crop and Chinese purchase patterns.

[By Sholom Sanik, June 1, 2023]

Chart 2 – CBOT July soybeans

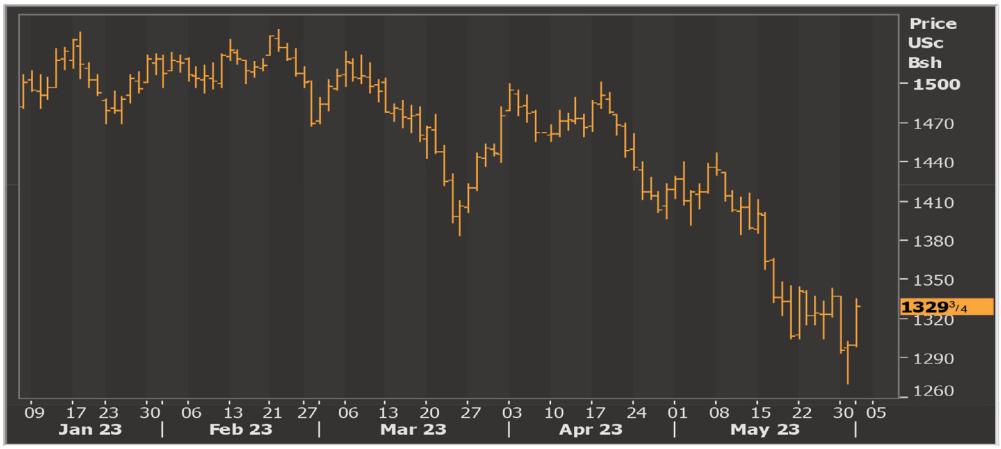


Chart courtesy Reuters

COTTON

A bull in hiding

The action in the cotton market is somewhat enigmatic. While corn and soybeans have responded to dry weather in the US with healthy rallies, cotton prices remain stuck in a rather boring eight-month trading range. Indeed, almost all diagnostics for the cotton market are constructively bullish.

Supply

As of the most recent USDA weekly crop progress report, 81% of the crop had been planted. That is below 89% last year at this juncture of the season and below the five-year average of 86%. The good-to-excellent portion of the crop fell from 51% the previous week, to 49%.

In the June crop report, the USDA revised its estimate for pound-per-acre yield, from 854 in its initial forecast for the 2023-24 crop, to 841. So, definitely not off to a great start, particularly in light of the fact that farmers were obviously not very optimistic about demand. US plantings are estimated at 11.26 million acres, down from 13.76 million acres last year.

To be clear though, despite last year's much larger planted area and excellent yields, the harvested-to-planted recovery ratio was a historic disaster. Final output was 14.47 million bales. Two years ago, in 2021-22, planted area was about the same as this year's with final output of 17.52 million bales (see *Focus on Futures*, April 28). If the weather situation stabilizes, production can still meet the USDA's forecast for 16.5 million bales. But there is a long summer ahead.

To boot, China, the world's second-largest cotton producer and largest importer, has experienced poor planting weather for its 2023-24 crop. Indeed, the USDA lowered its estimate for Chinese output by 500,000 bales in the June crop report, to 27 million bales, down rather sharply from last year's 30.7 million bales.

Demand

As we indicated on April 28, the USDA would need to respond to the strong pace of US exports. In the May crop report, exports were first raised from 12 million bales, to

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12.20 million bales. The June report then hiked the figure to 13 million bales.

The June 8 weekly export report showed a gargantuan 480,000 bale commitment. That's the largest weekly sales figure since September 2021. And for this late in the marketing year, which ends July 31, it's the largest weekly figure since June 2010! The bulk of the sales – 385,000 bales – were headed to China. The following week, exporters reported only 99,000 bales sold, but again it was mostly China taking 70,000 bales. Hence, the purportedly burdensome Chinese ending stocks, which alone represent 41% of global consumption, do not seem to be a huge factor as China continues to buy abroad.

Consider the following interesting statistic: While we are unlikely to reach last year's totals, we are definitely selling more to China than was believed possible. Only one month ago, total Chinese purchases (shipped and unshipped) from the US were 59.6% of a year earlier. With this week's report, that figure moved up to 73.6%.

Truth be told, we cannot offer any reasonable explanation as to why the market is so weak. The supply side is vulnerable, as illustrated. And China is buying.

On April 28 we recommended establishing long positions in December cotton, using a 77¢ per pound stop. Maintain the strategy.

[By Sholom Sanik, June 16, 2023]

Chart 3 – ICE December cotton

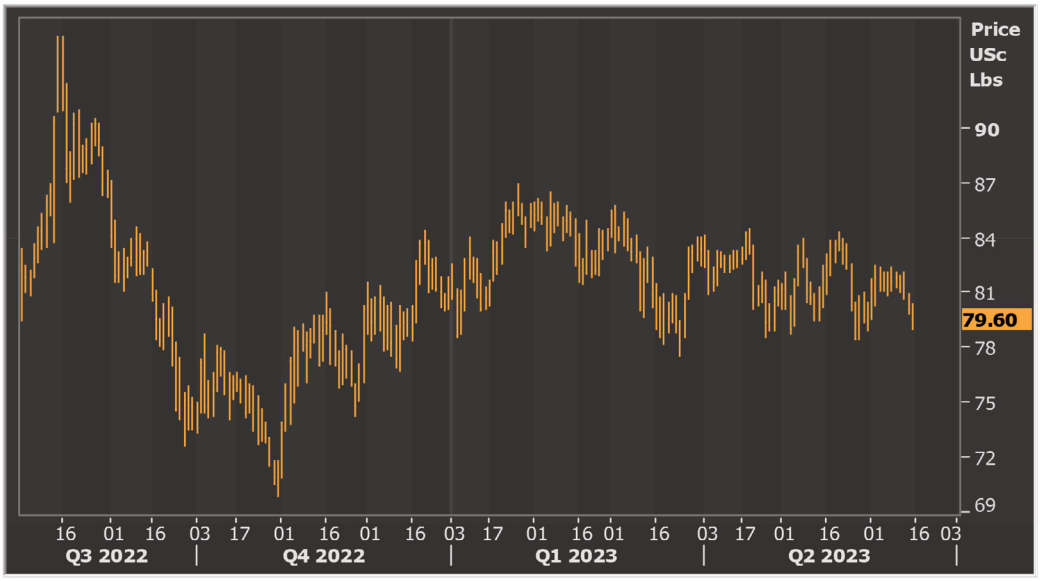


Chart courtesy Reuters

CORN

Is this drought an annual rite of summer?

Supply

When we last discussed the corn market (see *Focus on Futures*, May 5) we bemoaned the premature loss of our short position. In fact, July corn continued to plummet, by an additional 50¢ per bushel. We also cautioned that a long summer lay ahead. And indeed, before the 2023-24 US crop has even been fully planted, hot, dry weather appeared, sparking a massive rally (Charts 4 and 5).

At the moment, it is quite fair to say that the USDA jumped the gun on its yield estimate. The first estimate appeared in the May crop report and was not revised in the June report. The forecast called for 181.6 bushels per acre (bpa), which compares with 173.3 bpa in 2021-22 and above the record yield set in 2020-21 of 176.6 bpa. Well, although there is ample time for recovery, May and June weather is critical, and we feel comfortable stating that 181.6 is not in the cards.

In our May 5 article, we wondered why US farmers were planting the second-largest number of corn acres in history when planting soybeans was clearly more profitable. However, the rally in new-crop corn prices outpaced the rally in soybeans (Chart 6), so that has changed, but only to a degree. Optimum yield potential begins to drop sharply for late-planted corn, so this may

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not be a huge factor for late switching. The USDA's June 30 planting update may shed some light.

One of the background bullish factors over the past few months has been the 2022-23 crop failure in Argentina. Output is expected to fall from 49.5 million tonnes in 2021-22, to 35 million tonnes. The mitigating factor was Brazil where production jumped from 116 million tonnes in 2021-22 to a record 132 million tonnes for the crop that is currently being harvested.

It is very likely that from a global supply perspective, traders lumped the three largest exporters together, rationalizing that with South America neutral – despite Argentina – and a stellar crop coming from the US, there will not be any supply issues to be concerned about. Depending on how the US crop turns out, that may no longer be true.

Demand

Global trade was anemic in 2022-23. Total exports to all destinations fell from 206.53 million tonnes in 2021-22, to 176.55 million tonnes. Were this to continue, there may not be all that much to worry about. Looking at US exports, old-crop new commitments and shipments are running at a normal pace for this time of year. Commitments stand at 38.6 million tonnes. With 11 weeks remaining in the marketing year, it is unlikely that we will reach the USDA target of 43.82 million tonnes. But there is nothing terribly new about that.

Looking ahead to the 2023-24 marketing year, US forward sales are about 3 million tonnes, which is about half of last year at this time, and only 20% of 2020-21, the year in which China emerged as a corn importer of note for the first time in history.

However, in tracking the USDA's angle on this issue, consider that prior to the 2020-21 marketing year, China purchased on average about 5 million tonnes abroad. In 2020-21 that figure exploded to 29.5 million tonnes. In 2021-22 and 2022-23 imports fell to 21.88 and 18 million tonnes, respectively. It seemed that the Chinese phenomenon was ending. For the upcoming 2023-24 marketing year, the USDA is forecasting that Chinese imports will bounce back to 23 million tonnes.

For now, even if the USDA is correct, there is no evidence that the US has any part in any Chinese importing plans. To date, of the 3 million tonnes of 2023-24 commitments referred to above, only 272,000 tonnes belong to China. Nonetheless, the USDA is forecasting that US exports to all destinations will climb to 53.34 million tonnes from 43.82 million tonnes. If the demand side bounces back to normal levels, a US crop failure could stir a fresh bull run.

In summary, there are two potentially new bullish dynamics that have appeared: The possibility of a much smaller US crop, and the end of the global demand hiatus.

We will not see a yield update until the July 12 crop report. We will, however, get a feel as analysts weigh in on how much damage was suffered.

As far as demand is concerned, we will need to see some evidence that the USDA's forecast for new-crop-year exports is materializing. Owing to the uncertainty, we will restrain ourselves from jumping on what may be a very bullish setup.

Remain sidelined, but stay tuned.

[By Sholom Sanik, June 20, 2023]

Chart 4 – CBOT July corn

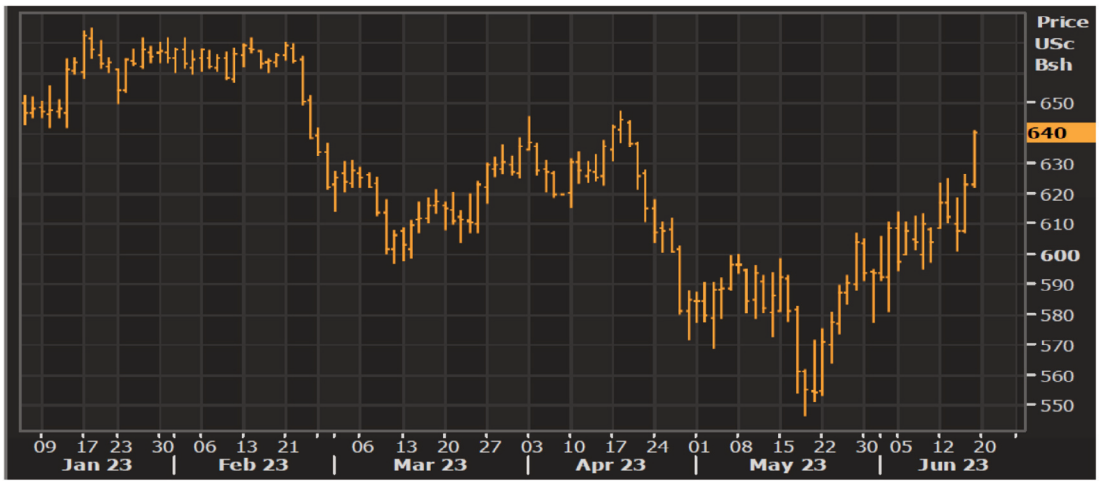


Chart courtesy Reuters

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Chart 5 – CBOT December corn

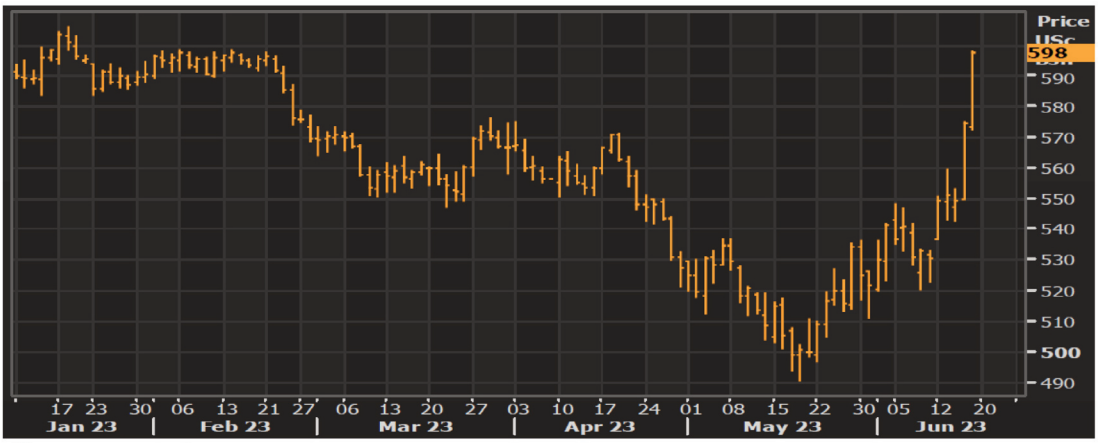


Chart courtesy Reuters

Chart 6 – November soybeans/December corn ratio



Chart courtesy Reuters

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