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Sugar: Fear the bear, not the bull

Sugar prices are trading as if a fresh set of bullish fundamentals had cropped up. Indeed, there are a number of developments.

There have been no changes for the supply side in Brazil. As has been the case since the crushing season began in April, there has been no letup in the swing away from ethanol production in favor of sugar. The most recent data show that 47% of the cane crop has been used for sugar, compared with 36% last year.

A bullish item that appeared in the bi-monthly industry report was that for the first time this season, ethanol sales for the first two weeks of September were the same as in the comparable period last year. Typically, sales have been 5% to 15% lower. It would actually be a bullish factor if it turned into a trend. However, in the near term it will not make much difference in the amount of sugar Brazilian processors will produce this year. We're very close to the end of the crushing season, and most of the cane has been processed. Estimates for total Brazilian output vary, but are all in the neighborhood of an off-the-charts 40 million tonnes. That compares with 29 million tonnes last year. An uptick in ethanol demand, were it to occur, would not matter much.

Another area that has inspired bullish sentiment is India. Production estimates for the soon-to-begin 2020-21 crushing season have been rising. The monsoon had its weak moments but overall will facilitate a major recovery to over 32 million tonnes, up from last year's off year of only 26.5 million tonnes.

The problem is that while the Brazilian harvest is fully automated and requires only minimal human labor, 90% of India's crop is cut by hand. This is stoking fears that migrant workers, who are relied on to harvest the crop, may be fearful of travelling while the risk of contracting the deadly Coronavirus still exists. It will be difficult to know how real this concern is until the harvest actually gets underway and difficult to say how it will impact output, but it is certainly adding to bullish sentiment.

There are differences of opinion in how the pandemic is going to affect global consumer demand. Forecasts for 2020-21 range from no effect at all with demand up 2% to down 2.5%.

However, what we do know is that we are looking at a massive influx of new supply that will be available for world trade. The uncertainty surrounding Indian production makes it impossible to quantify how much new-crop global output will rise. But with Brazil alone, we should expect an increase in global production that is greater than even the most optimistic demand forecast.

As such, we continue to believe that this rally will run out of steam sooner or later. The March 12¢ puts we recommended buying on June 19 are trading at 25% of their purchase value. For new positions, buy March 13¢ puts, presently trading at about 50 ticks. Hang in there, the bear should return.

[By Sholom Sanik, Sept. 27, 2020]

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Chart 1 – ICE March sugar

Chart courtesy Reuters

CORN

Is China's appetite insatiable?

While the 2020-21 US corn crop was being planted this past spring, corn prices fell to four-year lows because of large acreage, premier planting weather, and concerns over a sharp, Covid-related drop in ethanol usage. With the harvest now well under way, most of those losses have been erased, and prices are back to pre-pandemic levels.

The dynamics of these three catalysts have all changed. At the time, early projections for corn area were for 98.1 million acres, but are now estimated at 91 million acres. The great planting weather was compromised by poor growing weather. Finally, the recovery in petroleum prices has been projected to translate into a return to trend-line ethanol usage.

As the growing season nears completion, it is clear that a disappointing crop is no myth. Crop ratings keep dropping. The most recent weekly survey shows the good-to-excellent portion of the crop at a season low of 61%. With optimum conditions after seeding was completed in early June, that figure was 75%. The September USDA crop report estimated harvested area at 82.5 million acres, down from 89.6 million acres in June.

The demand side received a bullish boost from the September quarterly stocks report as well. September 1 inventories were estimated at 1.995 billion bushels, 254 million bushels lower than the average of analysts' estimates. This, of course, means that domestic consumption was much stronger than previously thought, and did not even include the barrage of Chinese purchases, the vast majority of which have not been shipped.

So, it's fair to say, at least as far as the US situation is concerned, the rally was well warranted.

Taking a closer look at China's sudden interest in US corn, unprecedented Chinese buying opens the question of whether we are at the doorstep of an entire new era that would deplete US inventories down to bull market levels.

Chinese consumption is well over 250 million tonnes, but imports have historically been negligible, averaging about 5 million tonnes over the past few years from *all* origins. Two factors contributed to the spurt of Chinese purchases. Drought will reduce the 2020-21 crop by about 10 million tonnes from 2019-20, which will leave a production/consumption deficit of about 30 million tonnes. True, China, according to official statistics anyway, has carried consistent ending stocks of about 200 million tonnes over the years, which should mean that the country can absorb a poor crop year. But then there is the other issue of meeting the government's commitments to the US-China trade agreement.

Thus far, China has committed to buy about 12 million tonnes of US corn for the 2020-21 marketing year. That compares with basically zero in years past.

The USDA estimates annual foreign sales to all destinations at a record 59 million tonnes. With current export flows, that seems to be attainable. Commitments stand at 25.8 million tonnes, compared with only 10 million tonnes last year at this time. But this forecast assumes a continuation of Chinese buying. And let's remember that most of these purchases were made when

US corn prices were much closer to $3 per bushel than where they are now – close to $4 per bushel. While the Chinese purchases have continued, there has been a noticeable slowdown. Some analysts have been saying that China is strictly a value buyer. As illustrated, any shortfall caused by the disappointing crop can easily be met with state reserves.

To put things into perspective, consider that the current estimate for 2020-21 global ending stocks is 25.8% of consumption. That compares with 28% and 26.8% in 2019-20, and 2018-19, respectively. During the 2017-18 marketing year, the high in spot corn prices was just over $4 per bushel – and that with ending stocks at 18.6%. Hardly a tight market. If China disappoints going forward, all the bullish US crop developments will still leave us with a well-supplied market.

We were stopped out of our short position in December corn at $3.57 per bushel, as per our June 18 recommendation. We now advise to reenter the short side. Sell March corn, currently trading at just above $4. Place initial stops at $4.35, close only.

[By Sholom Sanik, Oct. 15, 2020]

Chart 2 – CBOT March corn

Chart courtesy Reuters

COCOA

Waning demand

The first look at the new 2020-21 marketing year for the Ivory Coast shows port arrivals at 106,000 tonnes, down from 132,000 tonnes last year at this time. However, it is far too early to draw any conclusions. On the contrary, weather has been favorable for establishing subsoil moisture, and there is rain in the forecast for the foreseeable future. Conditions in number-two producer Ghana are similar. Forecasts call for both countries to top last year's output.

The recent sharp slide in prices (Chart 3) can be attributed to the demand side. Processors in all regions have not shown much confidence for a recovery in consumer confection consumption. Recently released grind results were dismal.

Third-quarter grinding in the EU fell by 4.7%, year-over-year. North America was 4.07% lower. And Asia was down 10.07%.

Over the past several years, a lot of grinding activity has shifted to origin countries, particularly in the Ivory Coast, where processing capacity has been growing. Ivorian grinding has been the lone holdout during the pandemic, showing moderate gains in the previous two quarters. But for the third quarter, grinding fell by 2.01%.

Product prices staged a recovery during the summer, but have now slipped. The butter ratio, which is the industry standard for gauging butter prices, has fallen to four-year lows (Chart 4). Even powder prices, which were quite strong in the early months of the pandemic, have been trending down since July. This leaves little incentive for bean processors to ramp up production.

The International Cocoa Organization's (ICCO) latest forecast for the 2019-20 global production/consumption balance was on August 31, calling for a surplus of 42,000 tonnes. Although traders were expecting a poor showing for the grind data, as mentioned earlier, they came in at the low-end of analysts' estimates. We anticipate that the ICCO's August surplus estimate was based on a more optimistic outlook as well, and as such, we believe that future surplus estimates will be materially higher.

Commodity funds, thus far, have been slow to react to the recent selloff. The most recent CFTC data show that they still own a large net-long position (Chart 5). And we see more liquidation down the road.

We are short December cocoa as per our September 8 recommendation. We advise lowering the suggested stop, from $2,700 per tonne, to $2,500, close only.

[By Sholom Sanik, Oct. 16, 2020]

Chart 3 – CBOT December cocoa

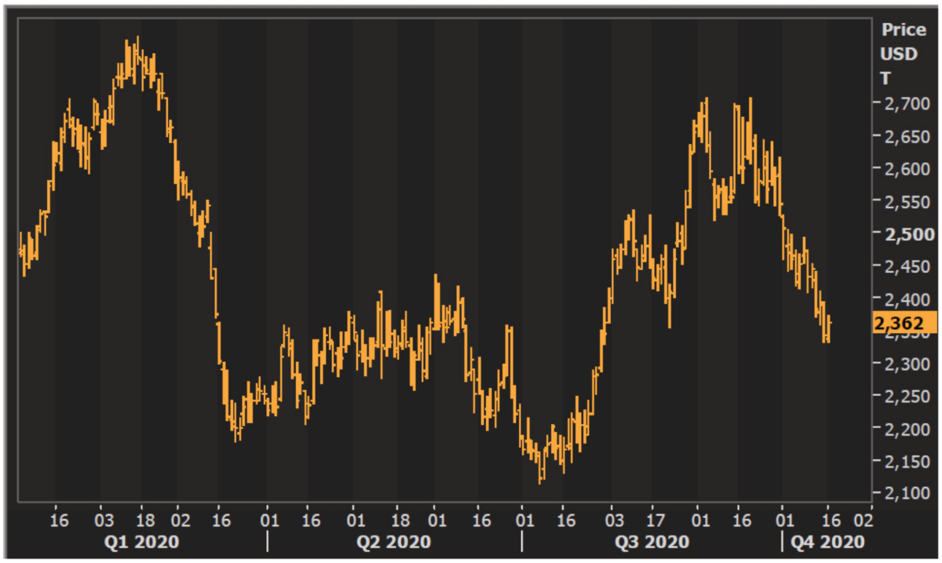

Chart courtesy Reuters

Chart 4 – Cocoa butter ratio

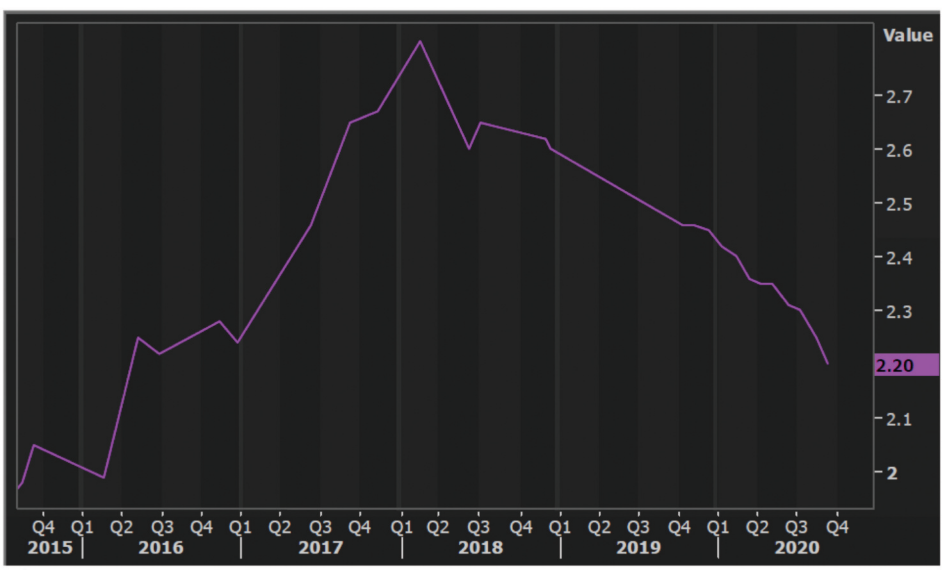

Chart courtesy Reuters

Chart 5 – CFTC net-long commodity fund position

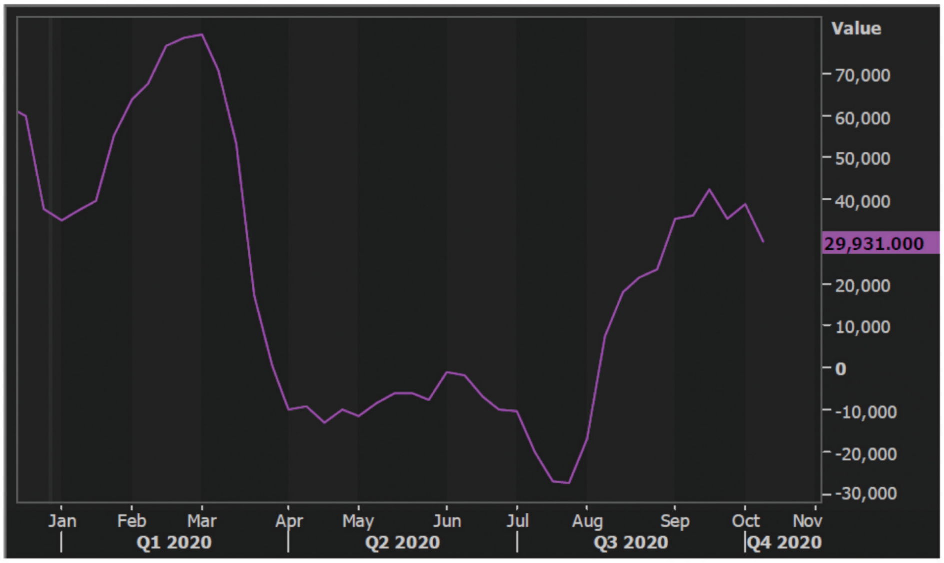

Chart courtesy Reuters

SOYBEANS

Chinese buying leaves the cupboard bare

Both supply and demand fundamentals for soybeans have turned decidedly bullish.

The overwhelming influence for this market has been Chinese imports. To date, China has booked 26.8 million tonnes of new-crop beans for the 2020-21 marketing year. This is a record for this point in the marketing year, which began on September 1 (Table 1).

The fact that sales have exceeded pre-trade-war totals is not in itself that meaningful for two reasons. The Chinese have some catching up to do after two seasons of absence from the US market. In addition, there is pressure for them to meet the goals set forth in the trade agreement they signed with the US. Nevertheless, they are whittling down what had become an extremely burdensome US stockpile.

Table 1 – Year-to-date Chinese imports

YEAR	IMPORTS
2020-21	26.8 MT
2019-20	7.15
2018-19	0.977
2017-18	17.13
2016-17	19.44

The November crop report added fuel to the bullish fire. In October, the US 2020-21 ending-stock estimate had fallen to 290 million bushels, already down dramatically from the unprecedented 909-million-bushel peak reached in 2018-19. The average of analysts' guesstimates for the November report was 235 million bushels, but the figure came in at 190 million bushels.

Despite the continuation of Chinese interest, the USDA stood pat on the export estimate, which is prudent because the pace of purchases is not likely sustainable.

After optimum US planting weather in the spring followed by excellent early growing conditions, the situation deteriorated rapidly with the onset of dry weather as the crop matured. The bushel-per-acre (bpa) yield estimate peaked at 53.3 in mid-summer, fell to 51.9 bpa in October, and was slashed further in the November crop report, to 50.7 bpa. That's about 250 million bushels below the August estimate and accounts for the nosedive in ending stocks.

Another bullish development comes from Brazil. China turned to Brazil at the height of the US/China trade war to meet its soybean needs, and as a result Brazilian exports in 2019-20 soared by more than 50% from a normal year, to over 90 million tonnes. The resulting depletion of Brazilian between-season supplies became a serious issue, as they have now turned to the US to meet domestic needs. A rare event. We are not talking huge volumes, but the headlines certainly beefed up the bullish sentiment.

The market has come full circle. US ending stocks have swung from 22.8% of consumption at the end of the 2018-19 to its current projected level of 4.2%. That's about as low as US inventories have ever been. During the same period, global ending stocks have fallen to 24% from 32.8%.

Looking ahead, South American planting weather has not been ideal and perhaps puts the fantastic estimate for a 7-million-tonne jump in Brazilian output to, 133 million tonnes, in jeopardy. In the November crop report the USDA already cut the Argentinean estimate by 1.5 million tonnes, to 51.5 million tonnes. But it's early, and the fact is that there has never been a South American planting season without a weather scare. Time will tell.

The very early USDA projection for 2021-22 US soybean area is 89 million acres. That compares with 83.1 million acres for this season's crop. Much depends on where prices will be when planting actually commences.

When we last discussed soybeans (see *Focus on Futures*, September 22) China's insatiable appetite for US soybean imports was front and center, but the extent of the crop damage was unknown. And who would have believed that Brazil would be buyer of US soybeans? We chose to be sidelined, leaving $1-per-bushel-plus on the table. While, as illustrated, the fundamentals are very bullish, we do not wish to chase, particularly since traders will soon turn their attention to the potential of massive new crops for 2021-22. Remain sidelined.

[By Sholom Sanik, November 12, 2020]

Chart 6 – CBOT January soybeans

Chart courtesy Reuters

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