BRAZIL DYNAMICS DRIVE SUGAR HIGHER

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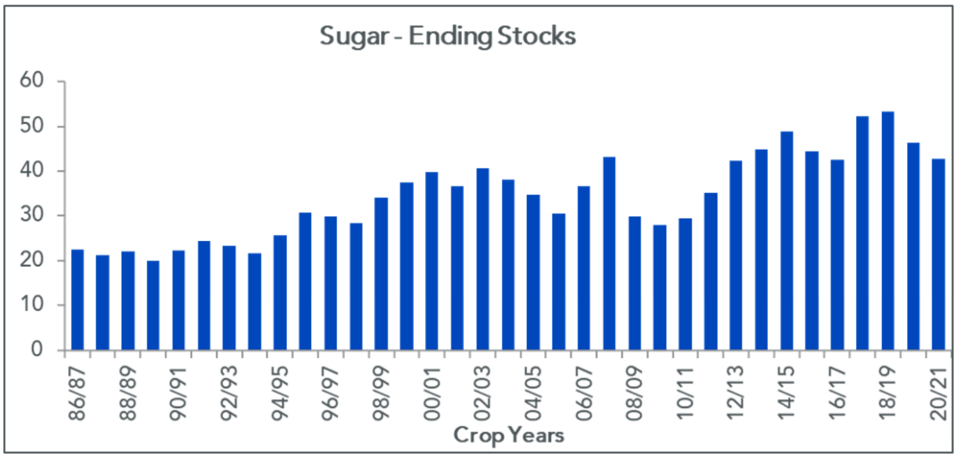
Sugar prices are up 14.2%[1] since the start of April 2021, mainly because the world's largest sugar supplier Brazil is likely to see a dip in production. Sugar, most of which is derived from sugarcane, is highly weather sensitive. Ideal weather conditions would entail a frost-free climate with sufficient rainfall during the growing season. Any weather condition that differs from this is likely to hamper sugar production, which would result in higher sugar prices. The dry weather that prevailed between August and October 2020 in Brazil damaged sugarcane fields, thus reducing production potential. Fire outbreaks also harmed cane stocks. Current weather reports expect dry conditions to persist into May 2021. The dry weather is also raising concerns that sugar cane yields in Brazil could be disappointing. The 33% reduction in processing figures in the main centre south Brazilian growing region are fuelling concerns. Amidst the current backdrop, Brazil's sugar production is expected to decline by 3mn tons Year on Year (YoY) to 35mn tons in the upcoming 2021/22 season. Brazil accounted for over 60% of the 2020/21 global raw sugar exports, any further negative developments as the peak processing season unfold in April could lend a tailwind for sugar prices.

Figure 1: Sugar Ending Stocks



Source: United States Department of Agriculture (USDA), Bloomberg, WisdomTree as of 20 April 2021. Annual data in million metric tons.

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According to the Commodity Futures and Trading Commission (CFTC), net speculative positioning in sugar has risen 7% since the start of April and is above its five-year average.

The recent strength of the Brazilian real is also lending buoyancy to sugar prices. The stronger real reduces the incentive to export sugar from Brazil, as profits in local currency decrease when sugar prices (which are invoiced in US dollar) are converted back into Brazilian Real. Consequently, producers are discouraged to offer more sugar on the export markets. Higher energy prices also raise demand for cane-based ethanol as an alternative fuel. Sugarcane is the among the most common feedstock used to make the fuel ethanol. Brazil, the world's second largest ethanol producer after the US, makes most of its fuel ethanol from sugar cane. Most cars in Brazil can run on pure ethanol or on a blend of gasoline and ethanol. The average sugar mix ranges between 34-48%. The recent rise in oil prices makes it more attractive for sugar mills to produce ethanol which competes with sugar. However, given the lower efficiency of ethanol versus gasoline, ethanol prices need to be 70% lower than gasoline to incentivise demand for the biofuel. As we head into the key summer driving season, we expect ethanol to benefit from higher energy prices.

Sources:

[1] From 6 April to 20 April 2021

[2] Sugar mix – ratio of sugar to ethanol allocated by the sugar mill

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