QSL Sugar Monthly Report

Current as at 10 October 2017

Sugar

Contract	Latest Settlement	Monthly Change	High	Low
Oct-2017*	13.54	-0.75	14.58	13.01
Mar-2018	14.00	-0.85	15.20	13.72
May-2018	14.11	-0.92	15.26	13.90
Jul-2018	14.29	-0.99	15.40	14.08
Oct-2018	14.64	-1.04	15.72	14.46
BRL/USD	3.1883	-2.84%	3.1996	3.0800
Ethanol Parity	15.11			

*Source: Bloomberg. Current as of 10.10.17 (*Oct 17 at end of contract on 28.10.17)*

What happened?

During early-to-mid September we experienced a recovery for sugar prices in the lead up to the Oct 17 expiry. Speculators bought back futures contracts to close out their sold positions and some Brazilian buying activity took place to enable more ethanol production. We also finally felt a bit of weakness in the AUD/USD. The net impact was that towards the end of September the prompt prices poked back above A$400/metric tonne (mt), and reached levels for the 2018 Season around A$440/mt at the same time. Over the past few weeks since then the market has fallen away again, with sugar prices falling and the AUD/USD strengthening.

From a fundamental point of view there were several reasons for the sugar market to be supported during the month. Firstly, there were a succession of hurricanes that ripped through sugar-producing regions in the Caribbean and USA. The impact is still being assessed, but it provided a supportive sentiment for buying activity in a number of commodities. Secondly, as shown in the table above, ethanol parity in Brazil remains higher than sugar. Typically, sugar trades at a premium to ethanol due to the delayed payment, so the current situation is expected to encourage a switch back from sugar to ethanol at some point and many analysts are sharing different scenarios for this which result in the current expectations for a global surplus to switch back to being closer to parity. The third fundamental reason is that Chinese smuggling demand is still very strong, which has led to record-high FOB (Free On Board) physical premiums for white sugar in the Asian region.

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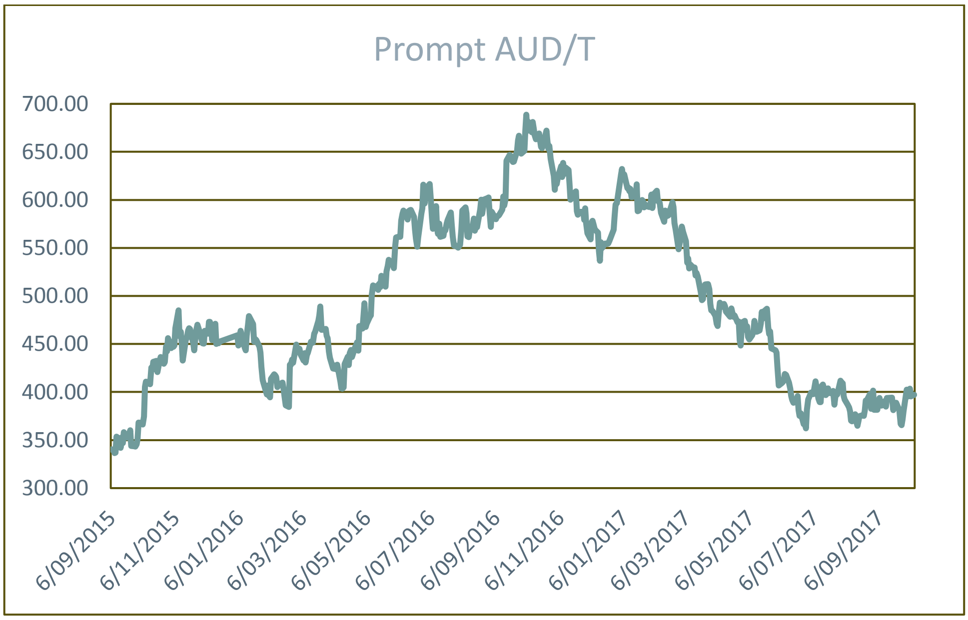
Balancing this relatively optimistic situation is the expected negative impact of growth in white sugar export availability from Pakistan and selling by producers coming from the new production recovery out of Europe and Thailand, India and China. The inability for Brazilian raw sugar to competitively access China and Indonesia due to tariff changes is also expected to weigh on the market.
The expiry of the Oct 17 contract was pretty tame compared to previous years, and there were no real surprises in the delivery volume of just over 1 million mt from South Brazil.

After continuing to buy back around 2 million mt of their sold positions sugar during September in the lead up to the Oct 17 expiry, the speculators have since piled back in, selling a massive 1.5 million mt back again over the past couple of weeks.



Source: Bloomberg. Current as of 10.10.17.

Going forward

The two opposing fundamental forces of excess white sugar in Europe/Pakistan and an improved crop outlook for Thailand, India and China versus the outlook for lower sugar production in Brazil due to the higher ethanol prices there are likely to keep the futures prices within a tight 13-15 c/lb range until either of these overpowers the other.

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With the mixed outlook for fundamental news, the newly increased speculator sold positions could potentially move either way and exacerbate a move to either side. A sustained breach of the technical indicators on the upside or downside could trigger further speculative selling or buying.

With the long five-month period lead up to the next futures contract Mar 18 expiry period, it feels like from the current spot market level of around 14 c/lb being a mid-point, we could potentially see pricing activity on either side of this level to test both ends of the 13-15 c/lb range over the next few months.

What could change?

Any USD strength (and corresponding Brazilian Real weakness) on the back of geopolitical issues could drive commodity markets down.

QSL Market Cost Drivers

MARKET COST DRIVERS	PROMPT (Mar 18) A$/mt as at 10.10.17	2018 Season A$/mt as at 10.10.17
Current Market	**$394.65**	**$420.65**
Sugar Fundamentals - Global exc. Brazil		
Sugar Fundamentals - Brazil		
Macro Issues/ Specs		
AUD/USD		

This report contains information of a general or summary nature. While all care is taken in the preparation of this report, the reliability, accuracy or completeness of the information provided in the document is not guaranteed. Information about past performance is not an indication of future performance and nothing contained in this report should be relied upon as a representation as to further matters. The update on marketing and pricing activity does not constitute financial product or investment advice. You should seek independent advice before making any pricing decisions. QSL does not accept any responsibility to any person for the decisions and actions taken by that person with respect to any of the information contained in this report.

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Currency

	Settlement	Range	High	Low
AUD/USD	0.7996	392 pts	0.8125	0.7733

Current as of 10.10.17.

What happened?

The AUD/USD continued to remain well supported above 0.8000 during most of September, even reaching up to over 0.8100 on the back of higher commodity prices and USA economic pressures and geopolitical uncertainty. However, in early October we finally experienced a sharp move back below 0.7800 with significant US dollar strength on the back of the much-anticipated Trump tax plan.

As expected, the RBA kept rates on hold during at 1.50% but speaking notes released after this suggested the RBA may be prepared to cut again if necessary. US data continues to print well. With a sustained media battle between the USA and North Korea around UN sanction packages, tensions have remained high and two missiles fired over Japan have prompted an early election there and calls for a stronger military capability.

Going forward

The USD continues to be net sold and exposed to any speculative buybacks. The US equities market continues to hit record-high levels and given the outlook for a further rate cut in Australia and potential for upside in the USA, the AUD/USD is still poised for further correction downwards. Now that some of steam has blown off the USD strength, our view is a little more moderated than earlier but we continue to see a 0.7600-7900 range for the next month or so, barring any geopolitical events.

What could change?

As outlined above, any developments in USA politics and North Korean/Russian tensions would impact the AUD/USD.