



Sucden Quarterly Market Report

Inside Out

July 2016



Agenda



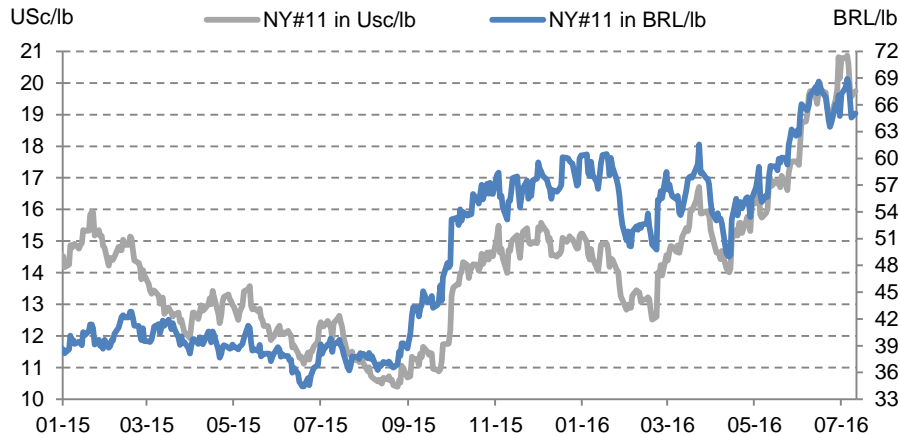
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The past 3 months in the sugar market

- From mid-April to 05 July, sugar prices increased impressively from USc14.0/lb to almost USc21.0/lb, a gain of close to 50% in less than 3 months. Out of 57 trading days, sugar was up 33 days, of which 26 by more than +10pts. Meanwhile, calendar spreads were also firm overall with, in particular, Oct/Mar trading near flat. Prices (and spreads) have eased since 05 July, now back to around USc19,8/lb. It is worth noting, also, that May/July and July/October both expired at a carry with 368 kt and 1,204 kt delivered respectively.
- While sugar prices were rising, the mood in the broader macro environment was clearly positive. Crude oil increased from \$44 to a peak of over \$52 early July, and the BRL strengthened from 3.50 to 3.22 end-June. Against this background, Funds bought heavily, adding 166,000 lots to their existing net long and reaching the striking record of +340,000 lots last week.
- During this period, fundamental news were also supportive: late rain virtually halted the crop in CS Brazil end-May/early-June and the line-up increased, the monsoon was late/slow in Asia, domestic prices in India and China strengthened thus endorsing news of the need for increased imports and rainy/cold weather slowed down sugar beet growth in the EU. This report examines the extent to which these news have tightened sugar fundamentals.

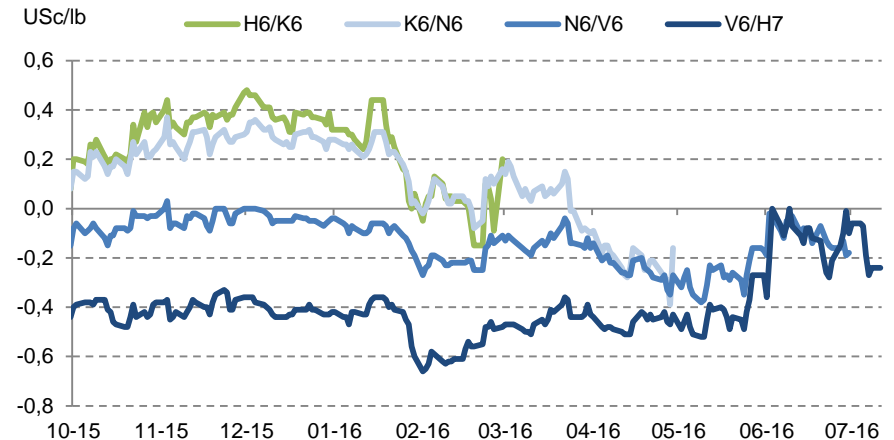
Sugar prices up to their highest level since 2012

NY#11 sugar prices in USD and BRL



Jul/Oct expiring at -18pts while Oct/Mar is close to flat

NY#11 sugar calendar spreads for 2016/17



CS Brazil

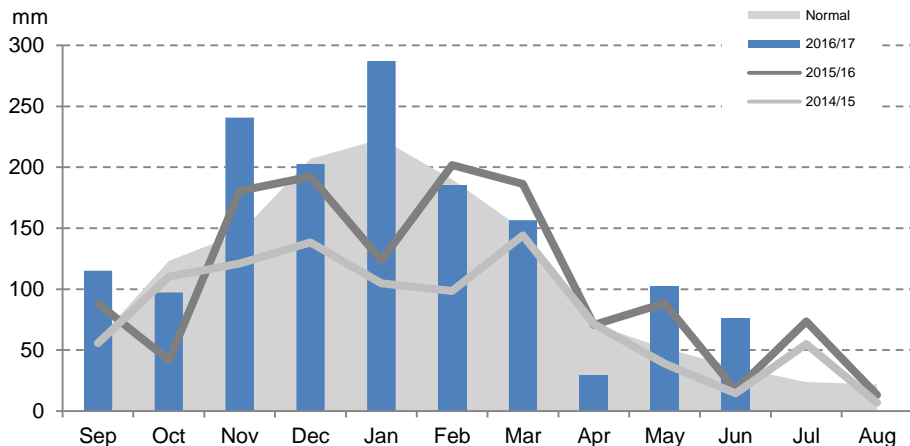
Weather hit after an ideal start

The start of the 2016/17 crop was impressive, early and benefiting from dry conditions. Sugar production was 2.6 Mt ahead of last year on 15 May. However, late rains end-May/early-June slowed down the pace of harvest and affected the ATR and the sugar mix. As a result, the advance decreased to 1.6 Mt on 15 June. A moderate frost event also hit the south part of CS Brazil early June.

- Late rains received end-May/early-June amounted to double the normal levels (100mm in May/75mm in June) and led to more days of crushing lost to rain (total of 10 days between end-May and early June vs 4 days normally).
- The impact was 2 consecutive “bad” Unica reports, for 2H May and 1H June: less cane crushed, lower ATR and a declining sugar mix. After an early and strong start, cumulated sugar production was 2.6 Mt ahead of last year on 15 May. The advance was reduced to 1.6 Mt one month later on 15 June.
- Early June, a brief and moderate frost event hit the south part of CS Brazil (Parana, Mato Grosso do Sul and south part of Sao Paulo).

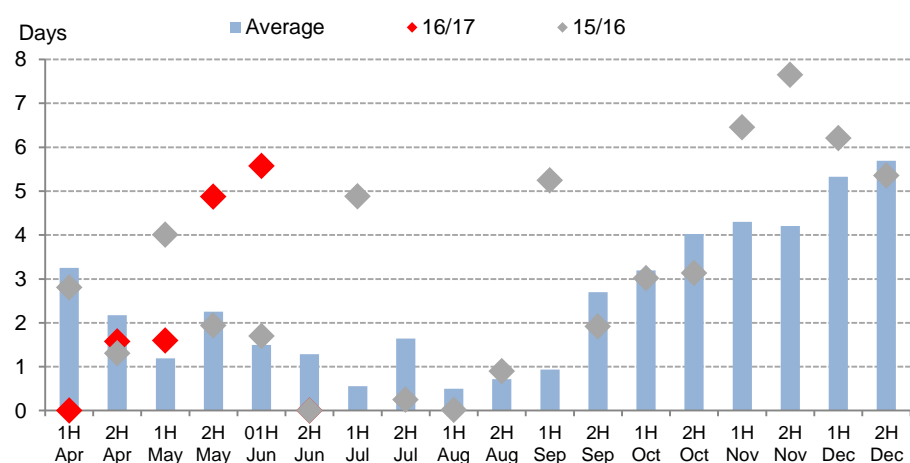
Late rains: double serving for May and June

Monthly rainfall in CS Brazil



And 10 days of crushing lost end-May/early-June

Crushing days lost to rain by fortnight



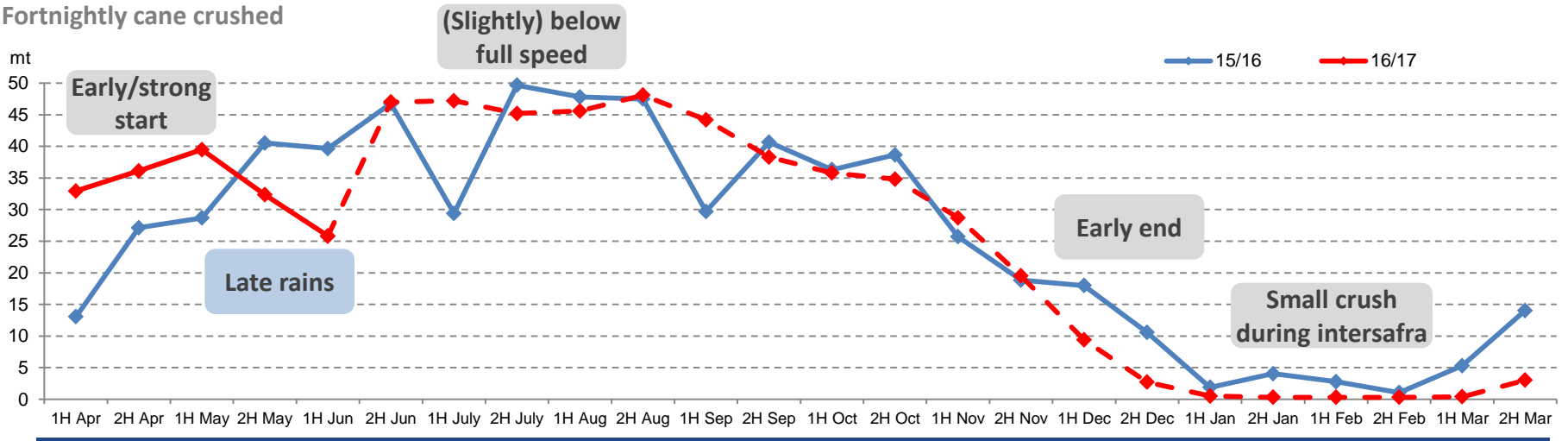
Cane crushed still on course for record level

The crush was slowed down end-May/early June by unseasonal rains. This said, the early start and existing industrial capacity would still allow cane crushed to surpass the record of last year. In fact, the limiting factor might be the availability of cane rather than industrial capacity. Given recent disappointment on Agricultural yields, there may be not more than 618 Mt of cane to crush in 2016/17 - same as for the record of 2015/16 - which would correspond to an early end of season.

- Agricultural yields decreased significantly in May (84t/ha) compared to the high level of April (90t/ha) and seem to be down further in June. The average of the season may be lower than last year while remaining at a good level at around 80t/ha.
- Available cane would amount to 628 Mt. However, given the strong crushing of Q1 2016, around 10 Mt of this cane would in fact be too young to be harvested by December in ideal conditions.
- As a result, cane availability may be the limiting factor for the cane crushed this season. At 618 Mt crushed, the end of the season would be relatively early with limited crush in December (in the absence of more unseasonal rain) even though the pace of crushing may be intentionally slow down slightly to allow sugar maximization.

The agenda for the 2016/17 crop

Fortnightly cane crushed



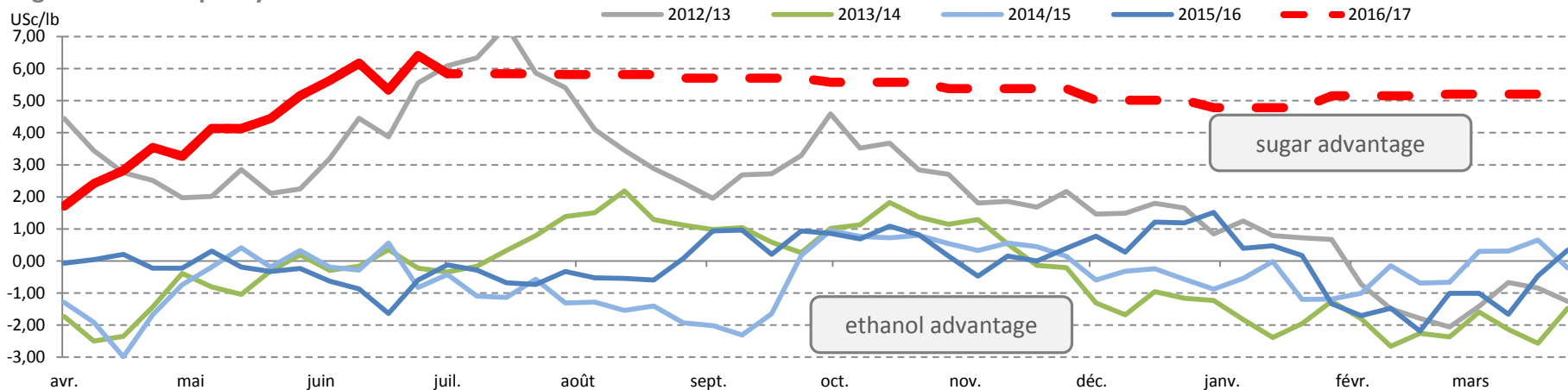
Strong sugar advantage over ethanol

The impressive rally in sugar prices drove sugar as much as 600pts above the ethanol parity during the 2nd-half of June. Economics will therefore push producers to maximize their sugar mix as much as crystallization capacity allows. Late rains that affected the mix during 2 fortnights will contribute to lower the average of the season. However, at 44.7%, the sugar mix would still be significantly above the level of 2015/16 at 40.5%

- Ethanol prices fell sharply when the season started in earnest. They rebounded somewhat when production was slowed down by rain but this came at a time when the BRL was weaker. The ethanol parity hovered between USc12,4/lb and USc14,4/lb (weekly basis) and the advantage of sugar increased from 170pts at the beginning of April to over 640pts end-June.
- This environment will obviously drive producers to produce as much sugar as they can.
- In this context, the sugar mix could reach 44.7% in 2016/17, significantly above the mix of 2015/16 at 40.5%. Sugar crystallization capacity seems to be a constraint preventing the sugar mix from increasing more. The late rains of end-May/early-June affected the mix during 2 fortnights and contributed to lower the average of the season.

Sugar 500-600pts above the ethanol parity

Sugar vs Ethanol parity: forward vision



Sugar output up significantly; new record likely

It seems that CS Brazil is on course to post a new record. It will be a close call for cane crushed which may end at the same level than the record of last year. However, given the foreseen levels of the ATR and the sugar mix, a new record for sugar output looks quite likely. At 35.3 Mt, it would represent an increase of 4.1 Mt year-on-year and would exceed the previous record of 34.4 Mt set in 2013/14 by a comfortable margin.

- **Cane crushed:** Industrial capacity is not the limiting factor; there is room to increase crushing activity in November and December in case of more disruptive rains before. Cane crushed could be higher/lower depending on how much cane is available (itself a function of the agricultural yield and the harvested area).
- **ATR:** mostly downside risks if the late rains of end-May/early June have a lasting impact.
- **Sugar mix:** will be maximized given the strong advantage of sugar compared to ethanol. Upside/downside risks from the below forecasts stem from the uncertainty as to what really is the max sugar crystallization capacity in a context where the sugar mix has not been maximized over the past 4 years.

Sugar output to increase greatly compared to 2015/16

CS Brazil historical crops and Sucden forecasts for 2016/17

		2012/13	2013/14	2014/15	2015/16	2016/17 05 July
Cane crushed	mt	533	598	573	618	618
ATR	kg/t	135,5	133,4	136,7	130,9	133,9
Sugar ratio	%	49,5%	45,2%	42,9%	40,5%	44,7%
Sugar production	mt	34,1	34,4	32,0	31,2	35,3
Ethanol production	mm3	21,4	25,6	26,2	28,2	26,8

But big variability linked to cane crushed and mix

Sugar output sensitivity to Cane crushed and Sugar mix

	ATR: 133,9	sugar mix										
		40%	41%	42%	43%	44%	45%	46%	47%	48%	49%	50%
600	30,6	31,4	32,2	32,9	33,7	34,4	35,2	36,0	36,7	37,5	38,3	
605	30,9	31,6	32,4	33,2	34,0	34,7	35,5	36,3	37,1	37,8	38,6	
610	31,1	31,9	32,7	33,5	34,2	35,0	35,8	36,6	37,4	38,1	38,9	
615	31,4	32,2	33,0	33,7	34,5	35,3	36,1	36,9	37,7	38,4	39,2	
620	31,6	32,4	33,2	34,0	34,8	35,6	36,4	37,2	38,0	38,8	39,6	
625	31,9	32,7	33,5	34,3	35,1	35,9	36,7	37,5	38,3	39,1	39,9	
630	32,2	33,0	33,8	34,6	35,4	36,2	37,0	37,8	38,6	39,4	40,2	
635	32,4	33,2	34,0	34,8	35,6	36,5	37,3	38,1	38,9	39,7	40,5	
640	32,7	33,5	34,3	35,1	35,9	36,7	37,6	38,4	39,2	40,0	40,8	

Brazil Ethanol

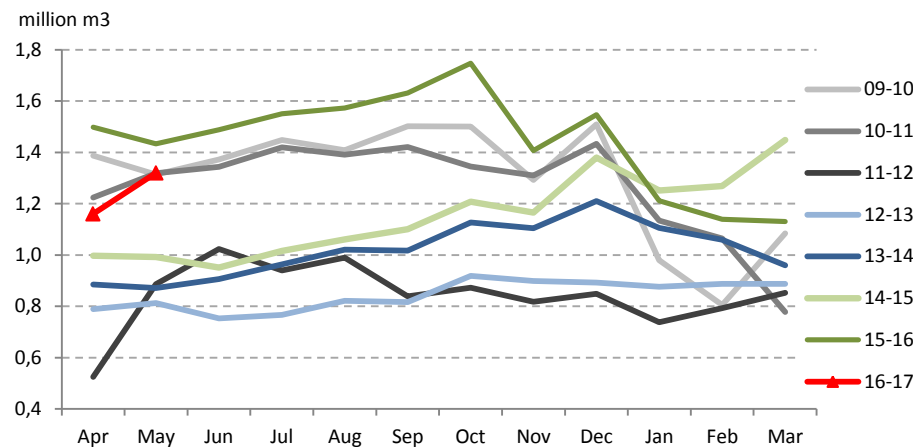
Domestic consumption heading to a new normal

After years of low consumption [1], demand for hydrous ethanol increased dramatically between February and October 2015 thanks to improved competitiveness and strong reaction from motorists [2]. Since then, demand decreased when prices were up [3] and recovered when prices were down [4] but drivers' interest for ethanol has increased in the process. It seems that demand going forward could stabilize at a higher level than in the past

- In May 2016, consumption of hydrous ethanol reached 1,320 km³ in Brazil, up 160 km³ from the previous month. It was however below May 2015 as the ethanol/gasoline pump ratio was higher.
- Going forward, the pump ratio may improve further in favour of ethanol but it is not expected to get lower than last year (as long as the regulatory environment is unchanged). As a result, hydrous ethanol consumption could ease slightly from 2015/16 while remaining at a high level. For CS Brazil, it could reach 14.4 Mm³, a decrease of 1.4 Mm³ from the previous record season (the April-May 2016 cumulated consumption is 360 km³ below last year).

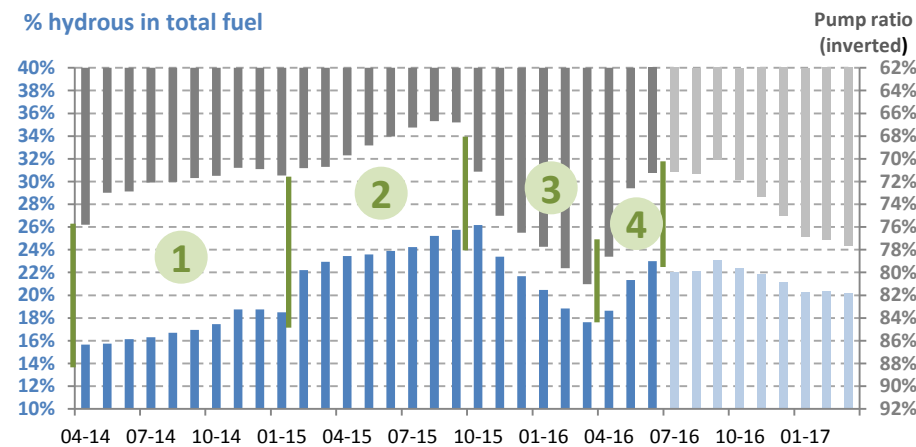
2016/17 ethanol consumption normalizing at high level

Monthly consumption of hydrous ethanol in Brazil



With hydrous share of pool above historical standards

Hydrous ethanol share (blue, left) vs Pump ratio (grey, right-inverted)



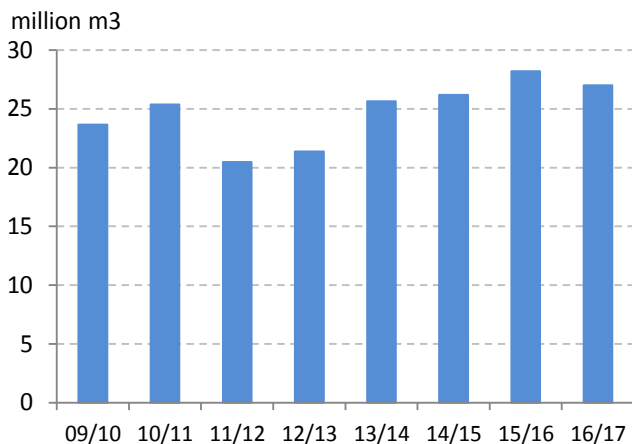
Balanced outlook but two-way regulatory risks

Declining production should be partly offset by easing demand and smaller exports. In the current regulatory environment, this results in balanced projected stocks. There are however two regulatory risks: one bearish in the event that ethanol loses its existing tax advantage at the end of the year, one bullish if gasoline prices are increased.

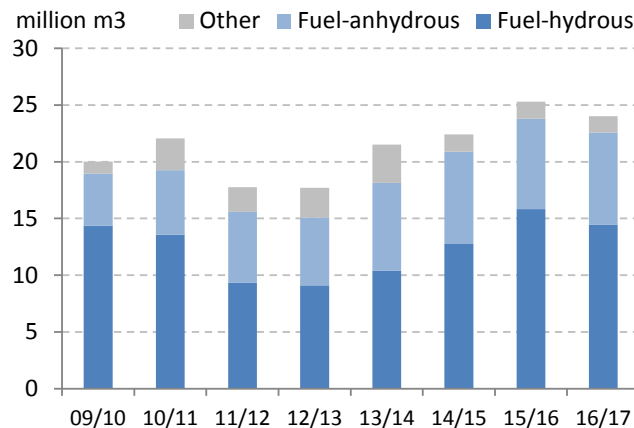
- In 2016/17, ethanol output in CS Brazil could decline by 1.2 Mm³. Domestic consumption could decrease by 1.4 Mm³ (as total fuel demand decrease) and exports could also get smaller as US origin represents cheap competition. Ending stocks are projected at 21 days of consumption which is balanced. Worth noting recently opened import parities thanks to the stronger BRL.
- There are distinct regulatory risks, one bearish and one bullish: 1/ The Pis/Cofin tax exemption benefiting ethanol is due to end in December 2016. In the absence of any extension (or the implementation of alternative measures), ethanol prices will increase at the pump and lose competitiveness. 2/ The new CEO of Petrobras suggested the possibility of increasing gasoline prices to align them better with international prices and to differentiate between states to account for logistical costs. Chances of increased gasoline prices have decreased in the short-term with the stronger BRL but if that happens ethanol attractiveness would improve. Also, there are lingering rumours of a possible increase of the CIDE tax on gasoline.

In 2016/17, production decrease to be offset by easing demand and smaller exports

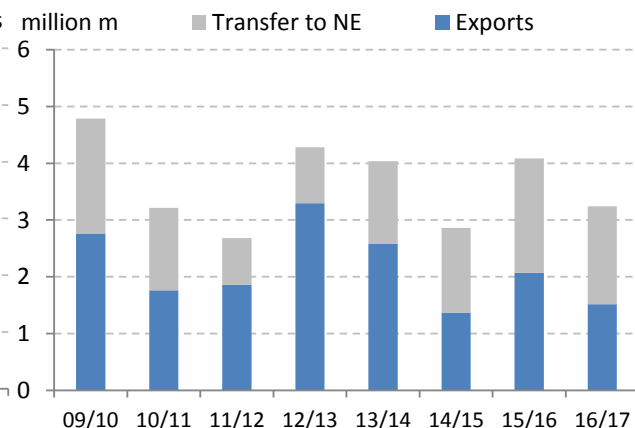
Production



Domestic consumption



Exports



Other Key Countries

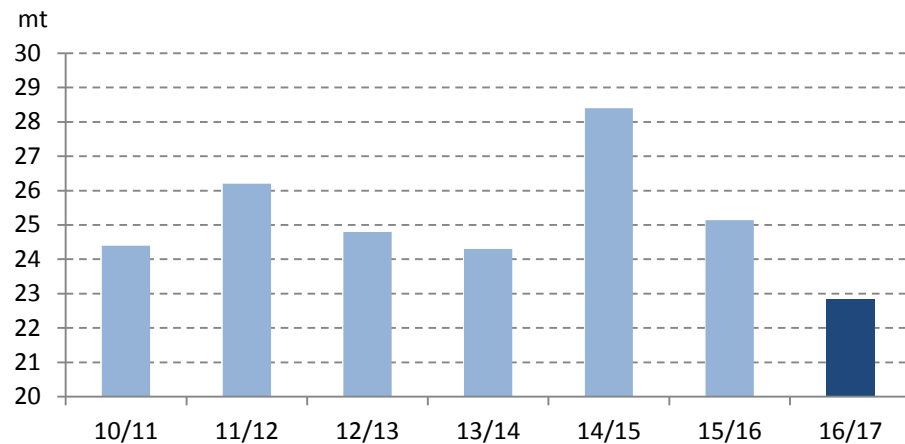
India: good monsoon needed

The 2015/16 crop which was affected by a weak monsoon will soon end around 25.1 Mt. All eyes are now on the 2016 monsoon which will be critical in determining not only the size of the 2016/17 crop but also the outlook for 2017/18 which heavily depends on the “Adsali” plantings of 16-month cane due to take place in August/September 2016. Assuming forecasts for an overall normal monsoon are correct, the 2016/17 crop is expected in a range of 22.5 to 23.0 Mt.

- 2016/17 production should be significantly down in Maharashtra and northern Karnataka which were hit by the poor monsoon of 2015; but slightly up in the northern states including Uttar Pradesh. India’s output should be in a 22.5 to 23.0 Mt range.
- Overall, the 2016 monsoon is forecast to be in line, or even slightly above, normal but with a late start. The start has indeed been disappointing so far, particularly in the sensitive area of Maharashtra where a good monsoon is crucial not only to allow a good cane growth but also to replenish water reservoirs which are currently at a low level.
- A good monsoon is also needed to allow cane area to recover in Maharashtra and northern Karnataka. Sugar prices are good and so should be sugar cane prices; and most of the cane arrears of 2015/16 have been cleared. The potential for a strong increase in the area for 2017/18 exists but is subject to a good monsoon to favour plantings and replenishment of water reservoirs.

A further crop decrease on the horizon for 2016/17

Sugar production in India (Oct/Sep, tel quel)



...Focusing on the west cane belt

India’s production by states (Oct/Sep, tel quel)

	2015/16	2016/17	Change
Maharashtra	8,4	5,8	-2,6
Karnakata	4,1	3,0	-1,1
Gujarat	1,2	1,1	-0,1
Tamil Nadu	1,4	1,7	0,3
Andhra Pradesh	0,8	0,9	0,1
Uttar Pradesh	6,8	7,7	0,8
Haryana	0,5	0,6	0,1
Punjab	0,6	0,6	0,1
Bihar	0,5	0,5	0,0
Others	0,9	0,9	0,0
India	25,1	22,8	-2,3

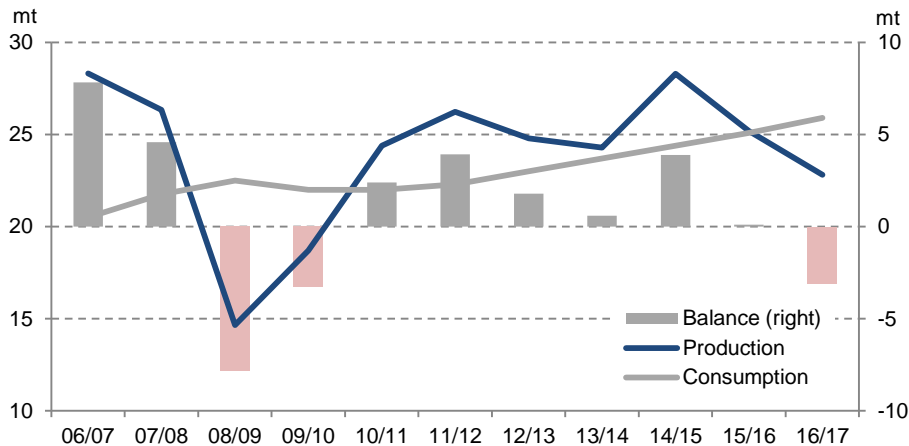
India: to import - or not?

India recently switched from subsidizing exports -to support local prices- to taxing them -to keep domestic prices in check. This was driven by the smaller crop (because of the weak 2015 monsoon) and by the rally in world prices -itself partly based on the threat of Indian imports. Whether India will import now relies on a combination of factors: parities, level of the comfort zone for local stocks, Government intervention...and weather.

- Indian exports are now ruled out. The smaller 2016/17 crop does not leave much room for exports and the Government, which is determined to keep domestic prices in check, has recently set up an export tax.
- While the smaller crop should leave a deficit of around 3.0 Mt in 2016/17, there are theoretically enough stocks to fill the gap. However, the Government might want to keep stocks at a comfortable level of around 3 months of consumption which may lead to imports of 0.5 to 1.0 Mt. For the time being, import parities are closed (even if custom duties are removed) and initial measures -such as stock limits- will aim at keeping prices under control (which will therefore maintain import parities closed)
- In fact, the coming monsoon should play a critical role: by determining the size of the coming crop and the one after, it will matter for the level of the comfort zone for the final stocks of 2016/17. This is a typical weather risk environment.

First deficit since 2009/10

India Production/Consumption [Oct/Sep, tel quel]



And rising prices that the Government will keep in check

India's domestic prices (NCDEX futures)



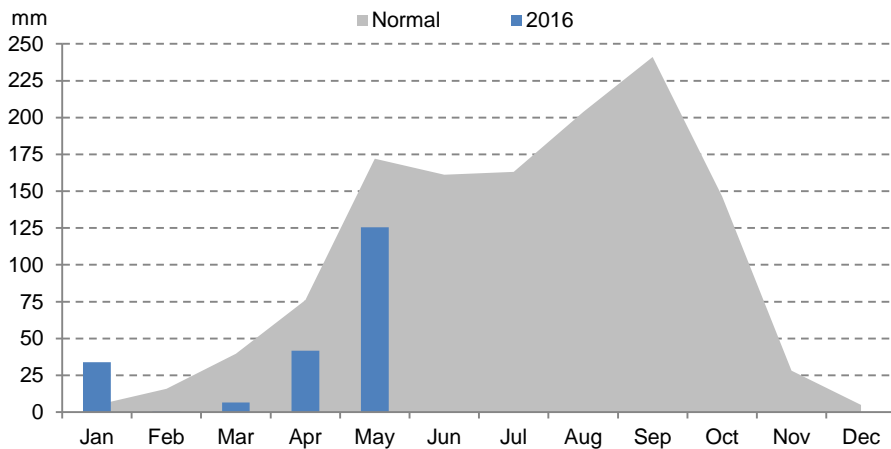
Thailand: 2 consecutive disappointments

The 2015/16 crop was disappointing at 9.7 Mt as it was affected by below-normal rain during the 2015 rainy season. The 2016/17 season did not start on favourable grounds either as the particular dryness of the dry season impacted growth potential. However, potential for recovery certainly exists if there is good rain over the next 3 months. For the time being, we assume a production of 9.6 Mt for 2016/17.

- The 2015/16 season finished mid-April one month earlier than the year before. Only 94 Mt of sugar cane were harvested (-11% compared to the 106 Mt of 2014/15) as agricultural yields suffered from below-normal rain during the 2015 rainy season. The sucrose content was also low at 10,4% but diminished conversion to ethanol offset some of the losses. Overall, sugar production at 9.7 Mt was a disappointing outcome.
- It is still early for 2016/17 as the 2016 rainy season has 3 months to go. The particularly dry dry season -combined with record high temperatures- hit the fields but potential for recovery certainly exists in the event of a good rainy season. For the time being, we assume 92 Mt of cane (below 2015/16) and a recovery at 10,5% that would lead to a sugar output of 9.6 Mt

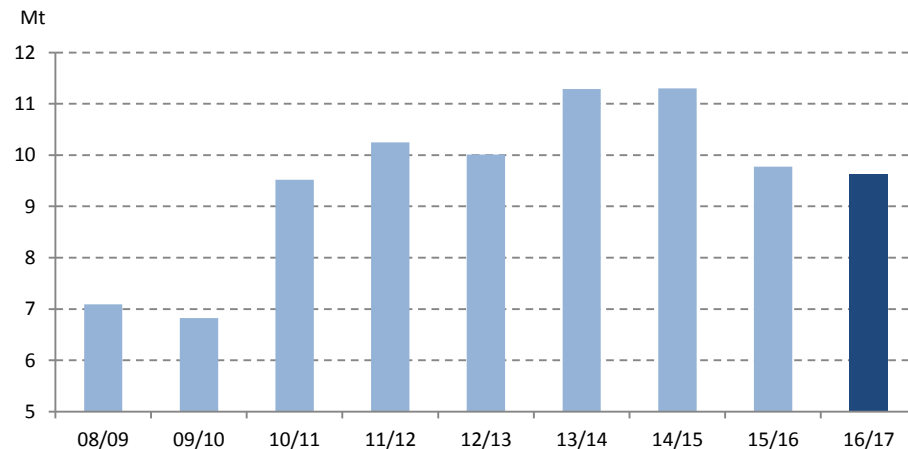
2016 dry season was...very dry

Monthly rainfall in sugar cane areas of Thailand



...and hurt prospects for 2016/17 crop

Thai production [Dec/Jan, tel quel]



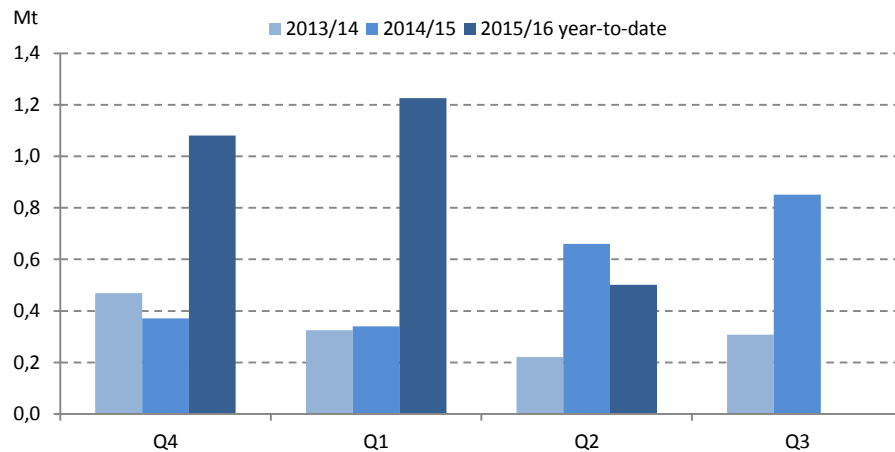
China: stable raws imports despite declining white flows

During Q2 this year, Chinese imports of white sugar eased after the impressive pace of the previous 6 months. Imports of raw sugar did pick-up but remained in line with AIL limits. 2016/17 imports of raw sugar should be stable compared to 2015/16 even though imports of white sugar should decline because of a higher crop and the assumed willingness of the Government to release some of its strategic stocks if/when domestic prices reach a certain level.

- Plantings for the 2016/17 crop finished in May. The acreage should be up 4,2% in Guangxi - and 3.5% for China - thanks to the improved price of cane. Spring and early-summer enjoyed above-normal rain which should favour cane growth. As a result, the 2016/17 crop is expected to recover strongly from the dismal level of 2015/16 at around 9.6 Mt.
- After 6 months at an impressive pace, imports of white sugar have eased in Q2. AIL raw imports were (will be) performed mostly in Q2 and Q3. In 2016/17, we expect AIL raw imports to remain stable thanks to a better crop and a potential release of strategic reserves -still limited to 2 Mt- which would decrease requirements for white sugar to 2 or 3 Mt.

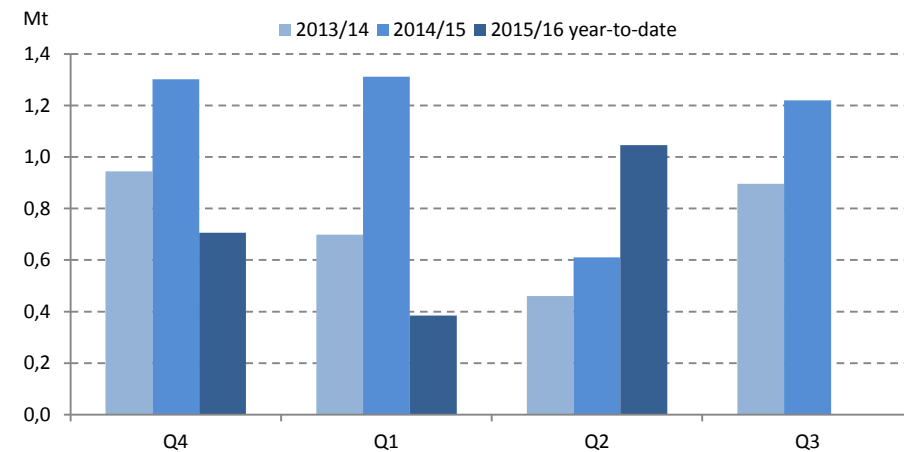
White imports easing after 6-month strong pace

China's imports of white sugar



And imports of raw sugar picked-up in Q2

China's imports of raw sugar



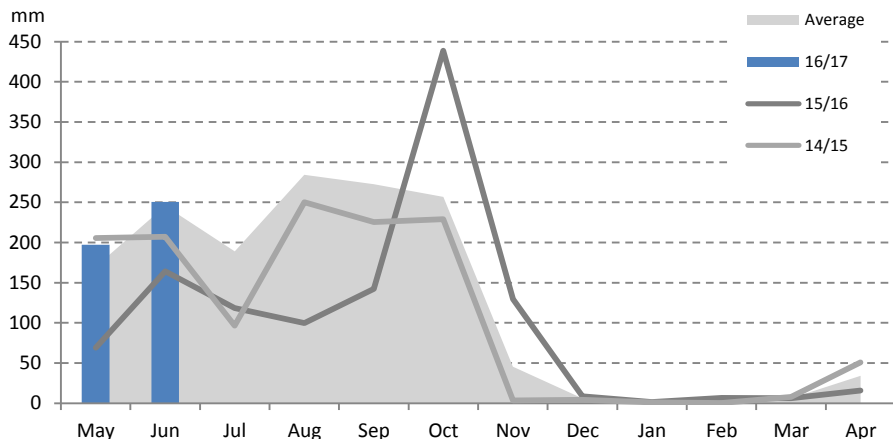
Central America: crop recovery expected

In 2015/16, Central America crops were hit by a disappointing rainy season and late rain and decreased by 440 kt compared to 2014/15. For 2016/17, although rain started slightly late, May and June were mostly normal. La Nina would bring above-normal rain if confirmed. In this case, Guatemala -where irrigation did help much last year- would be flat year-on-year but other countries would rebound. Total increase in the region could reach around 150 kt.

- The rainy season started slightly late with half the rain of May received during the last 5 days of the month. 1st-half of June was also slightly below normal in some areas. However, overall, May and June were still near normal.
- Guatemala: with La Nina the most likely outcome from August, concerns are actually more focused on above-normal rains and associated lack of sun (and possible hurricanes; although a low probability event). This could possibly prevent the crop from increasing given that, last year, lack of rain actually translated into decent agricultural yields thanks to irrigation.
- Other countries were hit harder last year by lack of rain given the lower irrigation capabilities. Conversely, crops would have more room to rebound this year, particularly in El Salvador which was the most affected.

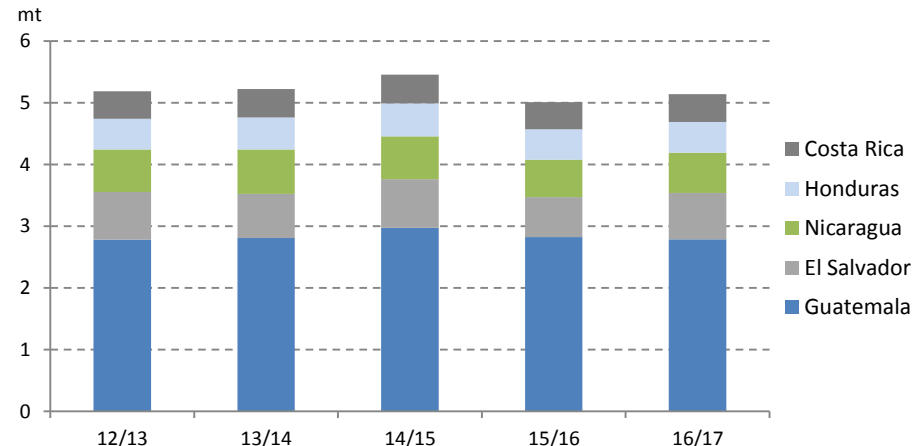
Rainy season starting more or less normally

Monthly rainfalls in Guatemala (Litoral area)



Central crops to recover from previous season's trough

Central crops and Sucden forecasts for 2016/17 [Nov/Oct, tel quel]



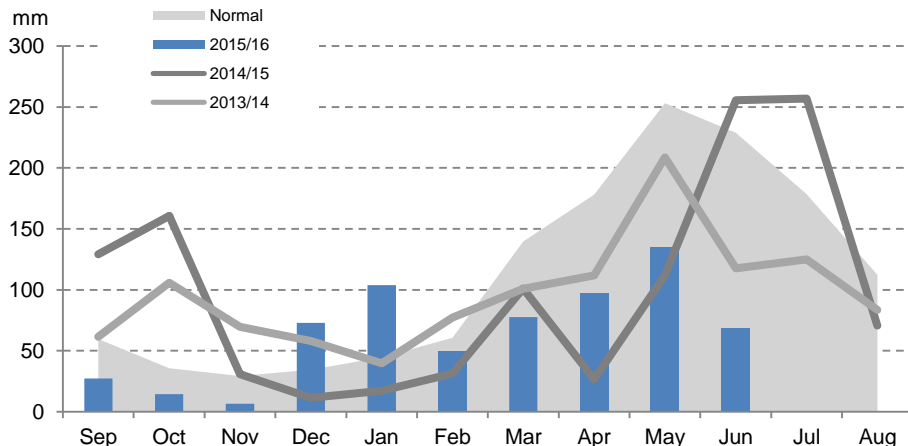
NE Brazil: more rain needed

The rainy season is roughly 50% below normal which should be a distinct concern. However, it seems that these rains are well split over time and allow the cane to escape severe stress. Consequently, a decent rebound compared to the dismal performance of last year can still be expected...subject to more normal rain during the two last months of the rainy season.

- Rainfalls has been below normal since the start of the rainy season in March, the cumulated of the past 4 months corresponding to roughly 50% of the normal. This said, these rains were well spread so far and alternated with sunny periods.
- This is probably what is keeping the outlook for the crop satisfactory, particularly when compared to the dismal performance of the previous crop.
- Overall, 53 Mt of cane could be harvested and lead to the production of 3.1 Mt of sugar, up 0.5 Mt year-on-year.

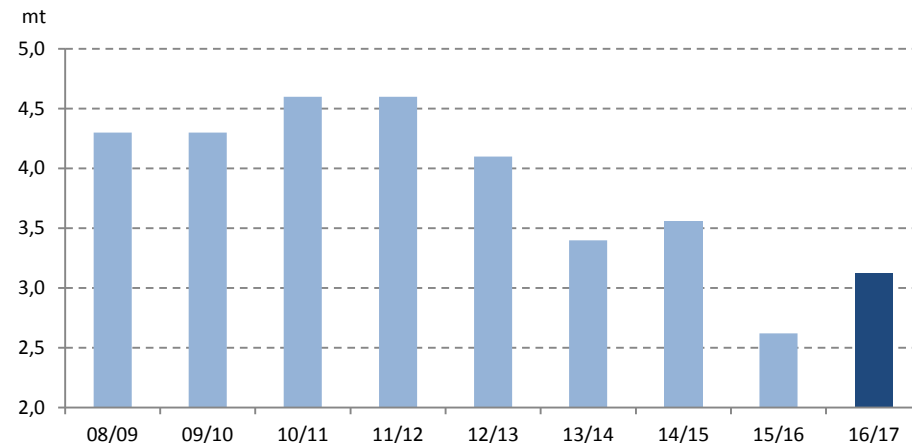
A disappointing rainy season

Monthly rainfall in NE Brazil



To cap the rebound from last year dismal level

NE Brazil crop and Sucden forecast for 2016/17 [Sep/Aug, tel quel]



EU: rebound to disappoint? – Russia: almost self-sufficient

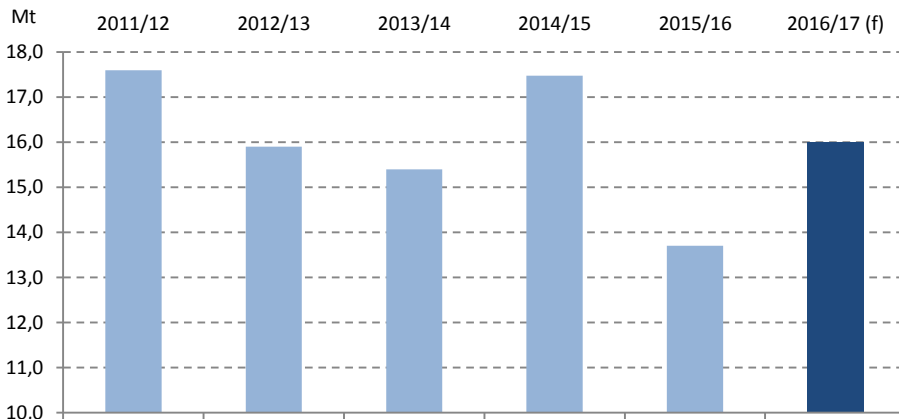
EU: after a very low crop in 2015/16, the 2016/17 output could be up substantially to around 15.5 Mt. This is however a disappointing rebound: the EU Commission recently published a smaller-than-expected area and the rainy/cold spring will have lowered the potential agricultural yield. Russia: crop prospects are very favourable and could lead the country to be almost self-sufficient.

European Union

- EU beet acreage increased but probably less than previously expected as pointed out by a recent release of the EU Commission. EU MARS sees agricultural yields up 2% from last year, and above the 5-year average. However, rainy/cold weather causes downside risks for France, Belgium and south Germany.
- EU sugar production could reach 15.5 Mt, a decent increase compared to last year but still somewhat disappointing.

EU sugar production rebound disappointing

EU sugar production [Oct/Sep, tel quel]

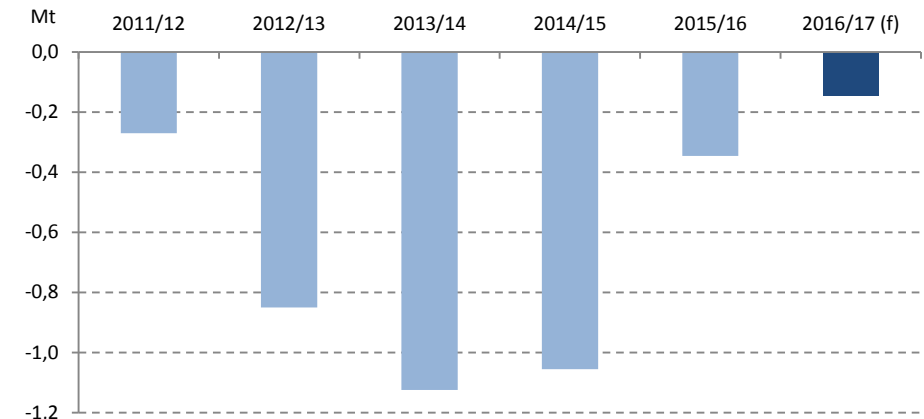


Russia

- After a record sugar production of 5.2 Mt in 2015/16, Russia could produce slightly more next crop with forecast at 5.3 Mt which would make the country almost self-sufficient.
- 1.08 Mha were sown early-June, almost 6% more than last year. And weather conditions are in favour of a good growth and a better beet yield. It may however lead to a lower sucrose content, particularly in southern Russia.

Russia near self-sufficiency

Russia sugar production deficit over consumption [Oct/Sep, tel quel]



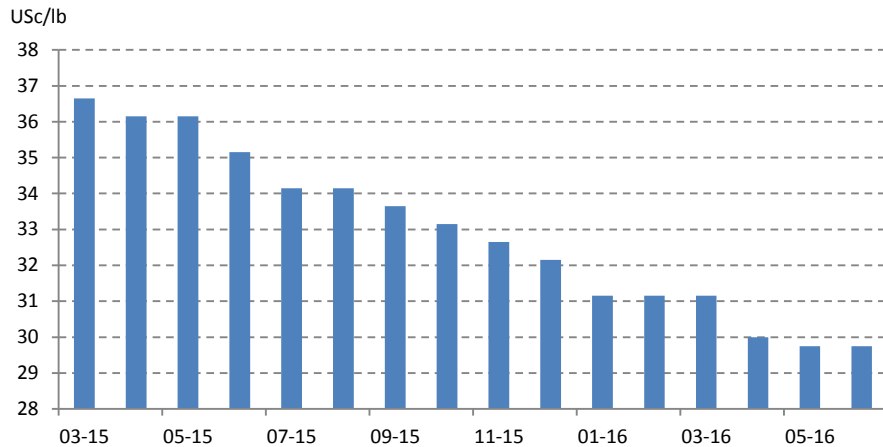
NAFTA: Is a sweetener trade war brewing?

As Mexican imports continue to bypass US Refiners, margins have fallen even further and the season may end with the largest divergence ever of raw vs. refined stocks. Short of CCC loan defaults for beet sellers, which are difficult given the political ramifications, there is little to suggest this scenario will change in the near term. In fact, all eyes are now on the US petitioners seeking amendments to the Suspension Agreements, the ramifications of which have 3 possible outcomes:

- I. No changes occur and the status quo prevails. Economics drastically reduce refiner run times, allowing the beet sellers to eventually clear inventories. Under this scenario the viability of the entire cane refining sector is questionable, however this is the reality currently playing out.
- II. Negotiations are successful and Mexico resorts to being a much larger supplier of raw sugar to the “traditional” cane refiners. Given that the current agreements have not yet been found to have been violated, this is a difficult scenario for Mexico to accept.
- III. Negotiations fail, the Agreements are terminated and AD/CVD duties are enforced. US prices and refining margins rally and the USDA is forced to either allow prices to rise to accommodate MX tariffs, or supply the market via sugar quota increases, leaving large surpluses in MX and raising the potential of a retaliatory HFSC lawsuit against the US, thus creating a larger trade war.

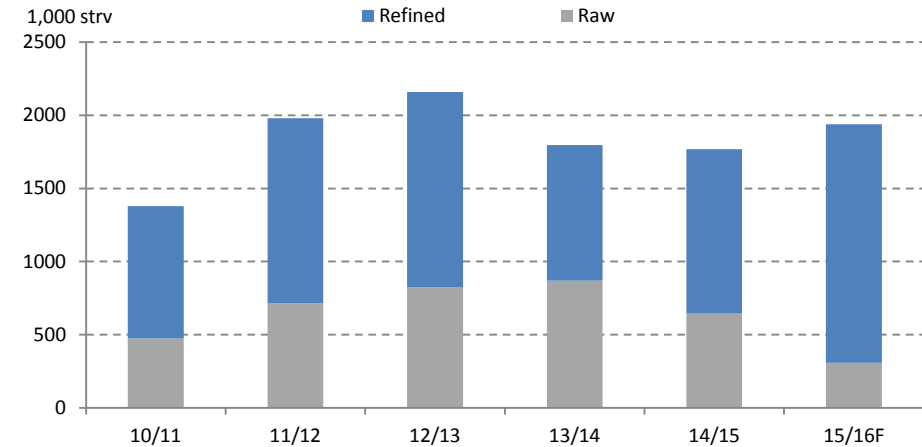
Crushing of the cane margin

Fob cane refiners equivalent for Chicago area



Largest-ever % variance of raw/refined stocks in the US

US end-of-season stocks (raw/refined split), 2015/16 projected



The World of Sugar

Global production: 16/17 set to rebound

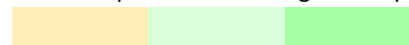
After 2015/16 saw a production loss of 11 Mt, key crops are expected to post a rebound of around 5 Mt in 2016/17. The bulk of the growth will be located in CS Brazil, the EU, China and possibly NE Brazil. Weather has been detrimental these past few months and decreased the potential for the final crop numbers: late rains in CS Brazil, cold in the EU, dryness in Thailand and, if persisting, a disappointing rainy season in NE Brazil. The Asian monsoon still needs to reassure.

2016/17 crops still set to rebound despite recent detrimental weather

Sugar production in key countries (local year, tel quel)

	Production	10/11	11/12	12/13	13/14	14/15	15/16	16/17
CS Brazil	Apr-Dec	33,3	31,3	34,1	34,4	32,0	31,2 (*)	35,3
Australia	Jun-Dec	3,7	3,7	4,3	4,4	4,6	4,8	4,9
Russia	Sep-Jan	2,7	5,0	4,8	4,4	4,4	5,2	5,3
EU	Oct-Jan	15,4	17,6	16,5	15,9	17,7	13,6	15,5
US	Oct-Mar	6,7	7,3	7,7	7,2	7,4	7,7	7,5
NE Brazil	Sep-Apr	4,6	4,6	4,1	3,4	3,6	2,6	3,1
India	Oct-Apr	24,4	26,2	24,8	24,3	28,4	25,1	22,8
China	Oct-Apr	10,5	11,5	13,1	13,3	10,6	8,7	9,6
Central America	Nov-Apr	3,9	4,7	5,2	5,2	5,5	5,0	5,1
Mexico	Oct-May	5,2	5,0	7,0	6,0	6,0	6,1	6,2
Thailand	Dec-May	9,5	10,3	10,0	11,3	10,8	9,7	9,6
Total		119,9	127,2	131,5	129,8	130,8	119,8	124,9

Crop scale: bad crop "normal" good crop



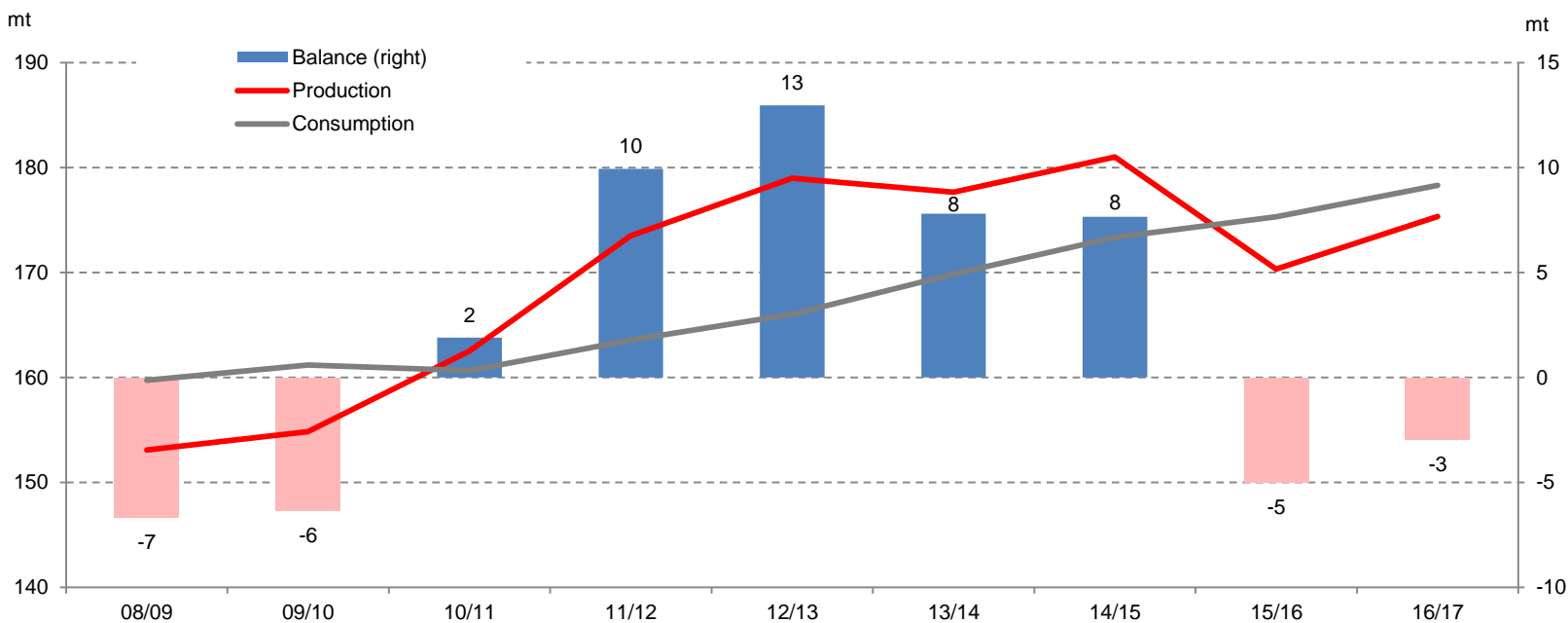
(*) cane plentiful but sugar mix lower

Global production/consumption: 16/17 deficit to narrow

Global consumption is expected to increase steadily by 2.9 Mt or 1.7% (so below the production growth expected in CS Brazil alone). Meanwhile, world sugar production could rise by around 5 Mt (less than earlier expected due to recent detrimental weather). As a result, the world deficit - which was substantial in 2015/16 and certainly ate into the previous surplus- could remain at a noticeable level around 3 Mt.

2016/17 projected deficit increased on recent detrimental weather

World Production/Consumption balance (Apr/Mar, raw value)



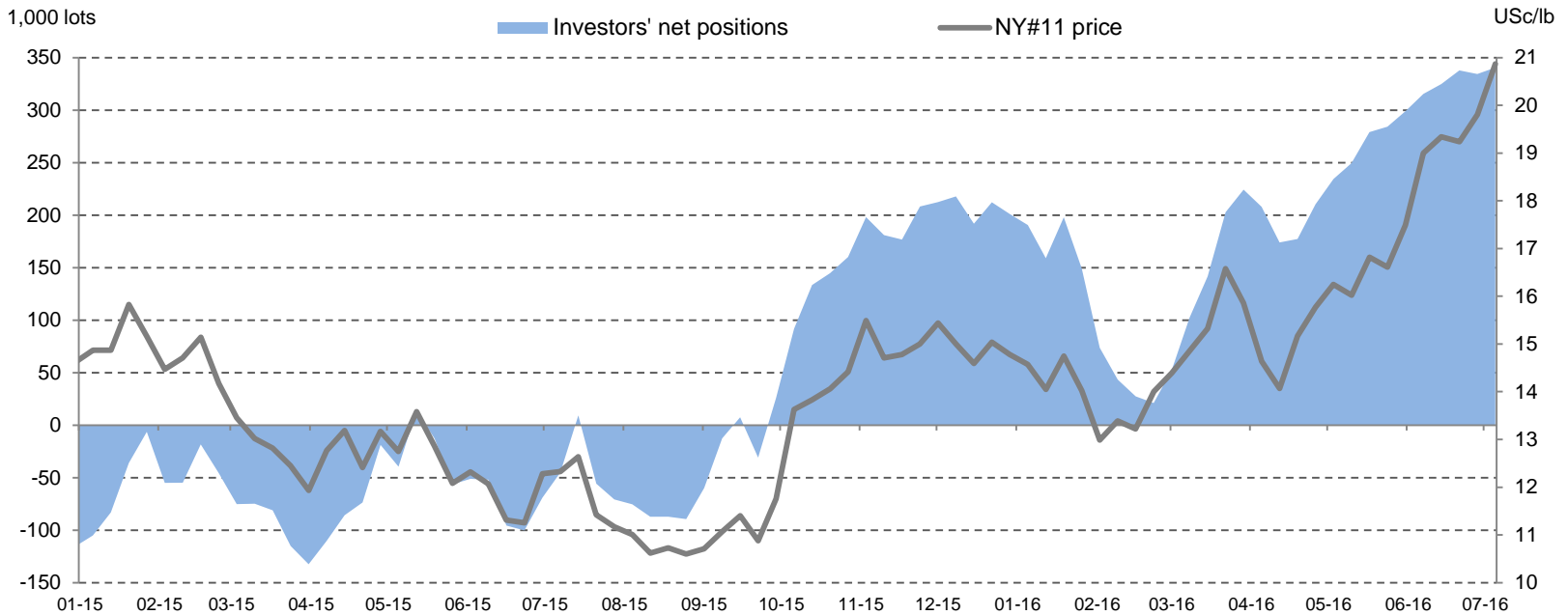
Mid-Term Outlook

CFTC report: Funds' net long grows to uncharted record

End-February, Funds were long a mere 21,000 lots of sugar. Since then, with only few exceptions, they have increased their position every week. Early May, they beat the historical record of February 2008 when they reached 234,000 lots...and rose much above this level afterwards up to 340,000 lots last week. This might be explained by a move of some investors from Index funds to more discretionary vehicles and therefore be of a more “structural” nature.

Funds' enthusiasm for sugar

Weekly Funds net positions



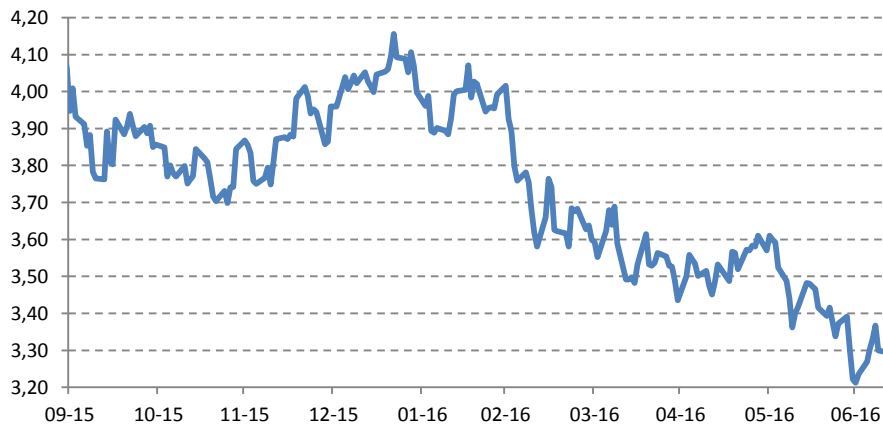
Macro environment: positive mood since February

Huge buying from the Funds was likely supported by a positive mood on the broader macro environment that started in February. Declining concerns over China, priced out US Fed rate hikes, rising crude oil prices and the impressive rebound of the BRL all contributed. Even the Brexit shock was quickly digested also thanks to expectations of strong stabilizing actions from Central Banks. Going forward, China's growth, dovish expectations on Fed and the EU cause risks.

- **BRL:** from 4.15 end-January to 3.21 end-June, the BRL gained 22% in 5 months. Drivers for this impressive rebound were a combination of domestic factors (impeachment, current account back to surplus, fiscal policy, carry trade, more hawkish Central bank) and international factors (declining worries about China, Fed rate hike priced out, rising crude oil prices, potential Central Bank actions). All these even allowed a quick and strong recovery after the Brexit shock.
- **Crude oil:** from \$30 end-January to \$52 early-June, crude oil (Brent) gained over 70% in 5 months before retracing. The main drivers of the move were supply disruptions/concerns in Canada, Nigeria, Kuwait and Venezuela which balanced the market sooner than expected. Even if fundamentals may switch back to surplus in the short-term when some of these disruptions end, a deficit is expected next year that should support prices going forward and allow them to reach \$60 by the end of 2017.

BRL staging an impressive rebound

USD/BRL exchange rate



Crude oil peaked at \$52

Crude oil prices (Brent)



Global weather: will La Nina help?

After the super El Nino of 2015/16, it seems that a switch to La Nina may take place as soon as in August. Typical impacts of La Nina are normally rather favourable for world sugar production bringing good rains in Asia and the Americas. But will La Nina be too late or lacking typical impacts? The monsoon was late/slow, the rainy season of NE Brazil is disappointing, that of Central America is barely normal so far.

- La Nina has become the most likely outcome for August with a 57% probability. The consensus forecast shows that SST anomalies would reach -0.6°C in August and -0.8°C in December. If confirmed, this event would therefore remain of a weak strength.
- Typical impacts of a La Nina event starting around mid-year would be positive for global crops: good rainy season in NE Brazil, Central America, India, Thailand, southern China (but lack of correlation in CS Brazil).
- For the time being, weather has had some detrimental impacts: late rain in CS Brazil, disappointing rainy season in NE Brazil, cold weather in the EU, late/slow monsoon in Asia. Although low probability, forecasts for hurricanes could also impact Central America

Switch to (weak) La Nina looks on the cards for August

Weekly sea surface temperature anomalies in Nino3,4 region



Outlook

- After a strong and early start, the crop in CS Brazil was virtually halted by late rain end-May/early-June. These will not impact the final cane crushed but the average ATR and sugar mix will be lower resulting in a net loss of sugar production. This being said, an expected final output of 35.3 Mt for 2016/17 would be a new record representing an increase of 4.1 Mt compared to 2015/16.
- In India, the crop will be lower than in 2015/16 -between 22.5 and 23.0 Mt- because of lower output in Maharashtra/Karnataka. This means that some imports should ultimately be required. Import parities are closed for the time being but the government will likely make sure to maintain final stocks at around 3 months of consumption (or 6.5 Mt).
- In China, the crop should rebound by around 0.9 Mt leaving a slightly smaller deficit. Thanks to the continuation of regional whites imports and to a potential release of governmental stocks, imports of raw sugar would be stable year-on-year.
- Elsewhere, there is a mixed bag of more or less good/disappointing crops. Overall, world production could increase by 5 Mt and the global deficit would persist at a noticeable level around 3 Mt (Apr/Mar, raw value). The trade flow surplus should remain substantial until the end of the year before declining somewhat towards a more shallow surplus at the end of Q1 2017.
- After a 1st deficit in 2015/16, another projected deficit for 2016/17 - even though a smaller one - will continue to eat into world stocks and balance markets. There is however no prompt shortage of sugar. Indeed, the July/October spread expired in a carry of -18pts and a delivery of 1.2 Mt which, without being specifically bullish or bearish in itself, at least proves that there is ample supply in CS Brazil. In fact, the strong rally in sugar prices - from USc14.0/lb mid-April to around USc20.0/lb now - should be put in the following context:
 - _ Detrimental weather has lowered initial crop prospects (or at least increased concerns) in key countries. This has logically increased the weather risk premium given that the Indian monsoon -in particular- still needs to reassure and that the projected trade flow surplus at the end of Q2 is somewhat shallow.
 - _ Weather issues came at the same time as an increase in the Brazilian line-up which may have given the impression of a stronger demand. However, the increase in the line-up was probably more due to logistical issues (rain, maintenance, dredging..) and to some demand anticipation. While Brazilian logistics is always a potential risk, it seems congestion was of a short-term nature and should ease soon.
 - _ The broader macro environment also instilled a positive mood as China's concerns declined, a Fed rate hike was priced out, crude oil rallied and the BRL recovered. Even the Brexit shock news was quickly digested. Funds bought sugar heavily as well as other commodities seen as an asset class with strong potential performances. Whether these purchases are of structural nature or will be reversed if/when the macro environment turns more negative, time will tell. Worth noting, in this respect, that while the positive mood of the market seems well-anchored, risks start to simmer from China, dovish Fed expectations and the EU.

THANK YOU!

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