S&D SUCDEN

SUCDEN SUGAR MARKET REPORT

DARKEST HOUR

OCTOBER 2018

EXECUTIVE SUMMARY

- Since May 2018, the world of sugar has gone through sizeable changes. Only a few months ago, the main producers' harvests were beating records and world S&D was seeing no end to an increasing surplus situation. Only a combination of bullish elements could have reversed the situation.
- Such elements have emerged. Weather events first, in Brazil and in the European beet belt which have seen their production forecasts cut. To some extent, Pakistan, Thailand and Central America also experienced less favorable climatic conditions than in 17/18. Low flat price has also contributed by lowering the CS sugar mix to an unprecedented level. Hence, by the start of 18/19, the paradigm of 17/18 when perfect weather and high flat price boosted production appears obsolete.
- Looking beyond, 19/20 CS gets lighter too with odds of a poor crop and a still-booming ethanol demand, provided strong crude oil prices and Petrobras gasoline pricing policy go on. 19/20 Northern hemisphere production shall also suffer from good alternative crops for sugar farmers, especially more remunerative wheat prices, so that limited but still meaningful reduction of beet & cane areas are expected.
- Consequently most countries have decreased their output and subsequent exportable surplus, or are about to. With the noticeable exception of India: Indian production has indeed jumped by 14 Mt in the space of 2-years and is enough to offset reductions elsewhere in the world. As a result India alone would hold more than 25% of world stocks by the end of 18/19 should exports do not occur.
- Market participants have been focusing so far on the Indian equation and funds have been riding the market from the short side for months now. However, with the reduction of the exportable surplus elsewhere in the world, Indian sugar exports are required to lighten the Indian balance sheet as much as to balance both raw and white world sugar trade flows. This could turn particularly critical during the inter-safra period when flat price cannot trigger immediate extra-supply through the CS sugar mix.
- Funds reversing their bearish strategy will be crucial for the world market to get back to a more constructive mood. Beyond resistance triggered by delayed producer pricing and Indian exports when parities versus the domestic market kick in, funds will need sustainable bull stories to keep the buying steam up. BRL and crude oil prices will have their barely predictable impacts, but more sugar-specific events could arise too. Perspectives of a lighter 19/20 S&D, the comeback of El Nino or tight inter-safra trade flows are amongst elements which could help the market to escape its current 10-year low range and get to brighter times.

AT A GLANCE

01 SUGAR CROP OVERVIEW

18/19 Centre-South Brazil: 9 Mt lower year-on-year
India: 2 massive crops in a row
Thailand: will the 17/18 record be repeated?
The EU: a bumpy climatic road for a crop failure
World crop year review: 17/18 paradigm obsolete

02 SUGAR MARKET FEATURES

Indian exports: weighing or required?
Brazil CS 19/20: the big call
Is sugar still an attractive commodity for farmers?
White market: back to square one
Order Flow: Funds shorting sugar for 18 months in a row

03 GLOBAL S&D

Is there light at the end of the tunnel?

SUGAR CROP OVERVIEW

18/19 CENTRE-SOUTH BRAZIL: 9 MT LOWER YEAR-ON-YEAR

A crop hit by harsh weather

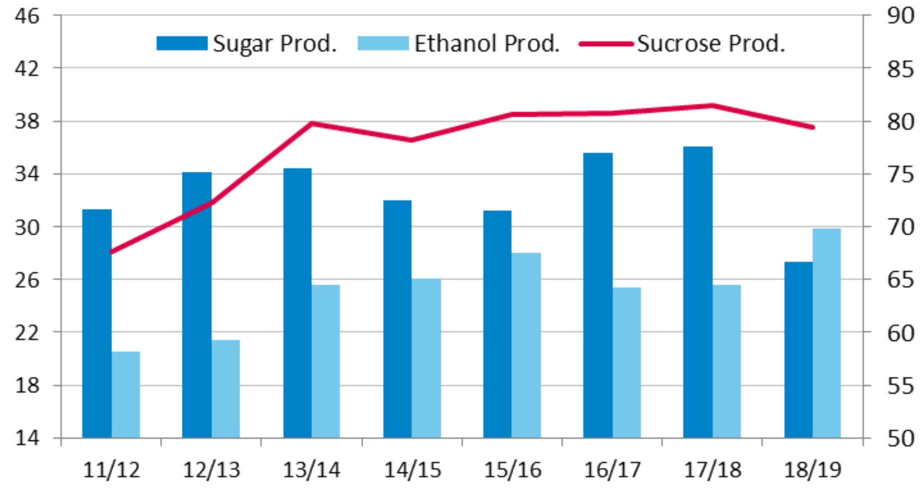
- CS cane growing season has been characterized by 2 consecutive drier-than-normal winters, leading to a 15% rainfall deficit in the overall cane growing development period.
- This hydric stress has reduced the potential yield by 5%, although it has not impacted the cane during its main growth.
- Low rainfall pattern during the harvest has nevertheless considerably increased ATR to levels unseen since 2010, and maintained sucrose production just 2% below last year.

Collapsing sugar mix

- The main feature of 18/19 was the extremely dynamic ethanol consumption boosted by the high gasoline-ethanol price spread. These record spread levels have been induced by three factors: high crude oil prices, Petrobras's gasoline price policy, and low sugar prices.
- Hence since the start of the crop, ethanol consumption is 20% higher year-on-year, while parity has always stayed in favour of ethanol.
- This situation has led producers to minimize the sugar mix as much as possible, to reach 10% below last year. CS sugar production should reach about 27 Mt, the lowest for the past 10 years.

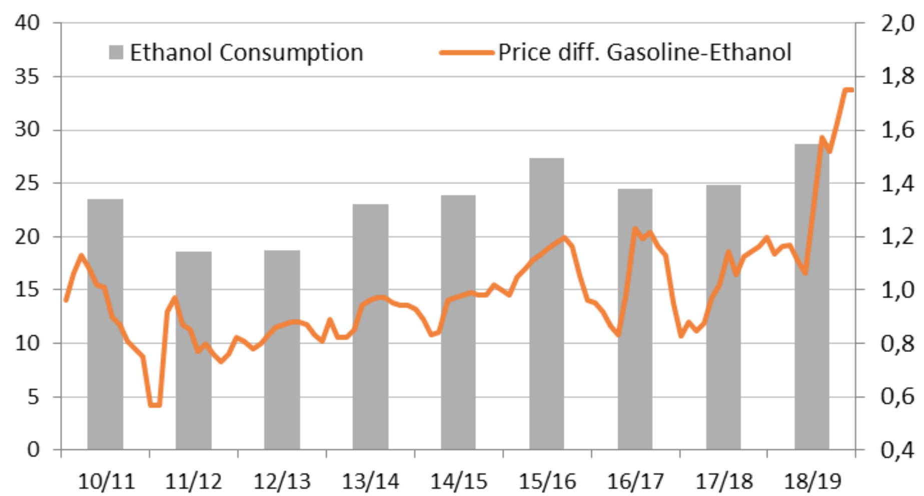
CS Brazilian production

[Apr/March, Left: Mt & Mm^3 - Right: Mt sucrose]



Brazilian ethanol consumption and price differential

[Apr/March, Left: Mm^3 ethanol - Right: BRL/L]



INDIA: 2 MASSIVE CROPS IN A ROW

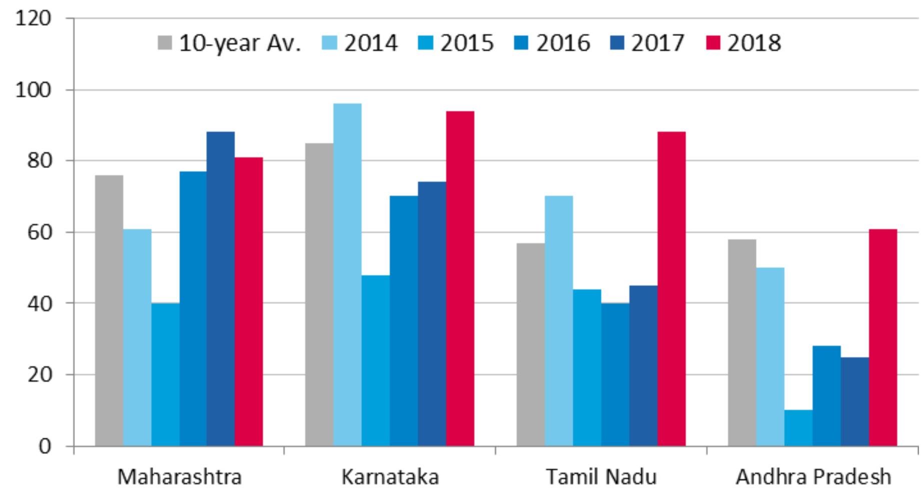
A favourable 2018 monsoon

- 2018 monsoon has proven beneficial for main cane areas, although yields are not expected to be as high as last year considering the older cane in Western India.
- The high current reservoir levels will support the standing crop during the dry season, and help plantings in Western India for the 19/20 season.
- 18/19 sugar production will benefit from some cane area increases, and despite lower yields year-on-year, it is assessed higher at 34 Mt.

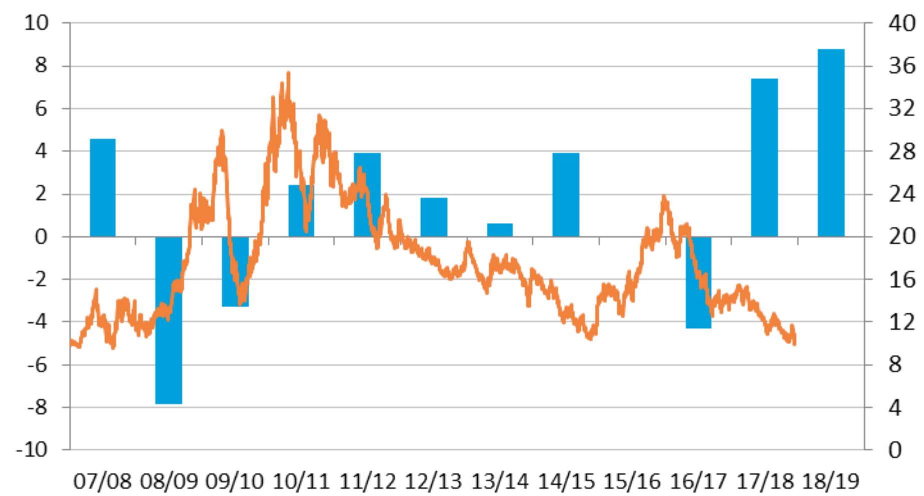
Unbearable stock-to-use ratio

- Two consecutive high sugar outputs will lead India to carry massive stocks at around a 70% stock-to-use ratio by end 18/19 should exports not occur.
- For cash-flow reasons and cane payments, mills will have to find new outlets outside of the domestic market even if they are less remunerative.
- The authorities are acting at multiple levers to sustain the domestic market, creating incentives for exports and ethanol production to help the industry's cash-flow and the mills to proceed with cane payments in a crucial election year.

Indian water reservoirs level
[% of storage capacity]



Indian production-consumption balance and NY#11
[Oct/Sep, Left: Mt sugar - Right: c$/lb]



THAILAND: WILL THE 17/18 RECORD BE REPEATED?

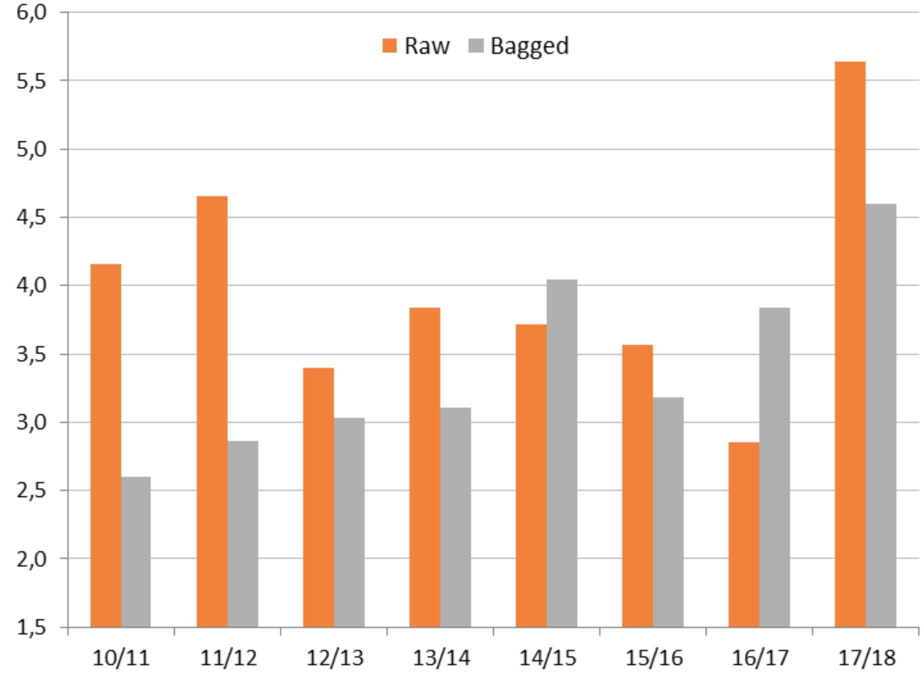
Monsoon less abundant than last year

- 2018 monsoon has not been as beneficial for cane as last year. It arrived earlier but the rains were less intense and more scattered.
- The cane yield is not expected to repeat last year's record but should still reach a high level, and lead cane production to be in the 125-130 Mt range.
- White sugar production should be favoured by mills, and remelt activity will be helped by large bagasse availability.

Exports finding homes regionally

- Raw sugar exports are expected at a record level, in line with the crop. They should flow exclusively to the region, mostly to the detriment of Brazil CS exports.
- White sugar exportable surplus shall also mainly remain in the Far East, benefiting from the large demand linked to China-related flows.
- Despite the large 17/18 crop, ending-stocks for both raw and white sugar should remain manageable and be either remelted or exported during the first months of the 18/19 crop.
- Far East demand has proven sufficient so far to absorb the new Thai production pattern, at the expense of Western Hemisphere sugar.

Thai sugar exports
[Dec/Nov, Mt sugar tel quel]



THE EU: A BUMPY CLIMATIC ROAD TO A CROP FAILURE

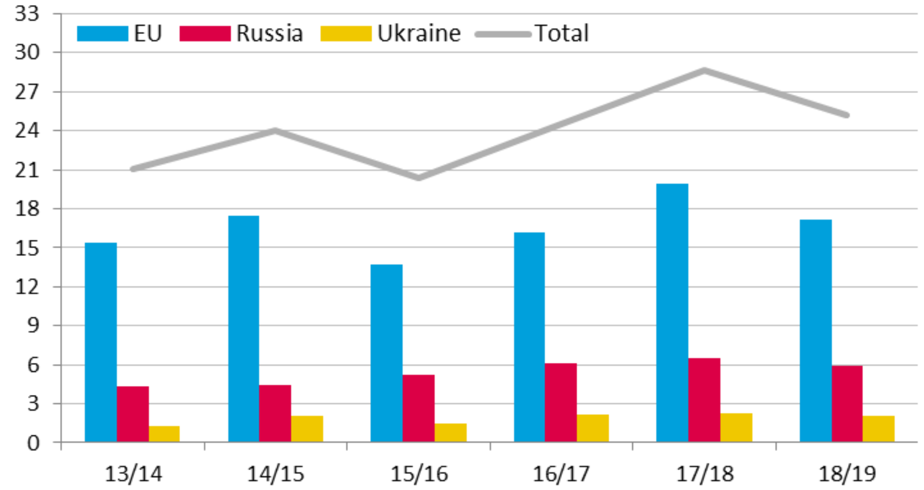
Detrimental weather

- The overall European beet belt has suffered from an extreme weather sequence in 2018: late sowing due to cold temperatures, favourable rainy & hot spring weather, and summer drought.
- The last 3 months' hydric stress environment will induce significant reduction of beet yields, only partially compensated by higher sucrose content. This season crop will also be characterised by a high heterogeneity in yield performances.
- All in, the European beet belt should mark a 10% crop reduction year-on-year, losing more than 3 Mt.

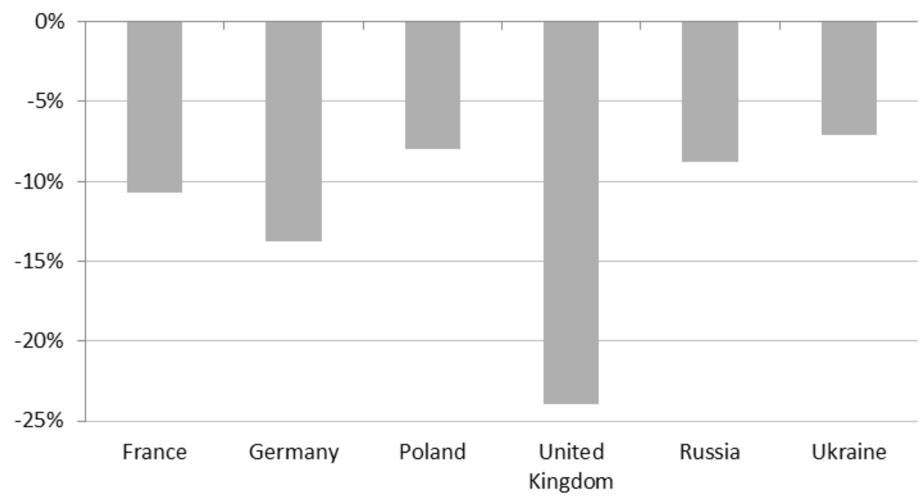
EU Exports level almost back to quota era?

- With reduced production, 18/19 EU exports should be halved compared to 17/18, making its contribution to the white market comparable to the quota era.
- Further, 5 to 10% of the beet area is expected to switch to more remunerative wheat alternative in 19/20. As a consequence, beet millers may also reduce their 18/19 exports to maximize carry-out with the current low flat price.

EU & Black Sea sugar production
[Crop year basis, Mt sugar tel quel]



2018/19 Sugar output variation versus last year
[%]



WORLD CROP YEAR REVIEW: 17/18 PARADIGM OBSOLETE

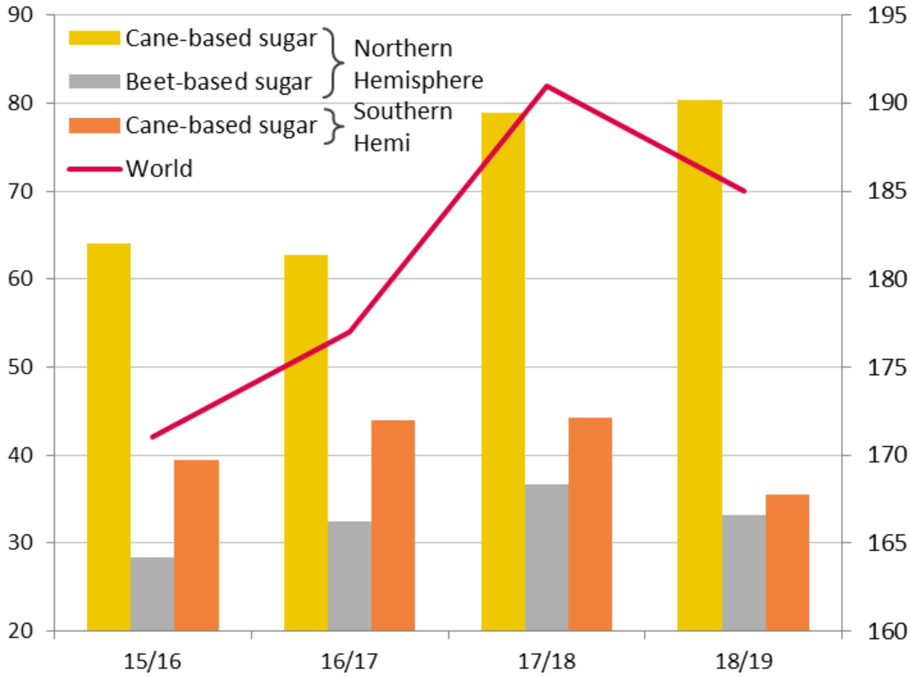
Weather events back and low flat price

- After worldwide beneficial weather conditions in 17/18, improving production in almost every country, and high 2016 sugar prices, pushing for better crop care and maximization of sugar mix in CS, the 18/19 environment has proven radically different.
- European beet belt has been struck by adverse weather conditions, as Brazil CS and Pakistan, driving to significant decrease of sugar production in these areas. India and Thailand are the noticeable where climate was not detrimental.
- Further, CS has again demonstrated its large flexibility in the mix adjustment to less sugar production in a context of low sugar prices and higher crude oil prices, making ethanol more profitable all through the campaign.

19/20: the tipping point?

- 19/20 will start with several unfavourable features: dry winter in CS lowering the 19/20 cane yield potential, resilient high crude oil prices, high wheat prices and neonicotinoid ban in the EU, lower crop in Pakistan, low flat price hitting the Thai potential…
- Can India compensate for all of this?

Sugar production per feedstock and hemisphere
[Oct/Sep, left: Mt sugar – Right: Mt Total World production]



SUGAR MARKET FEATURES

INDIAN EXPORTS: WEIGHING OR REQUIRED?

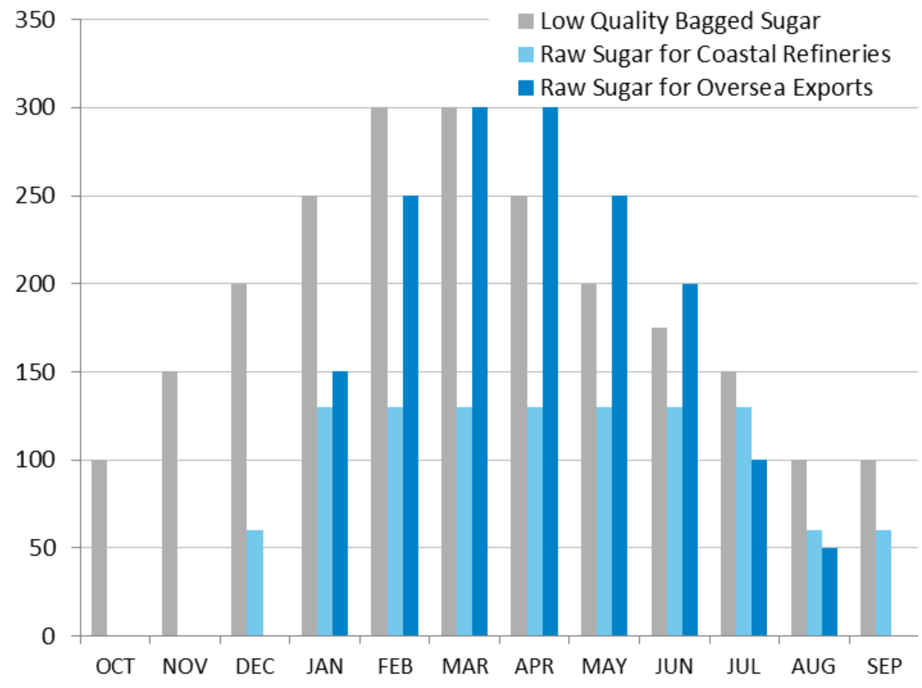
The multiple Indian scenarios

- The Indian exports are required to avoid unbearable stocks-to-use ratio and will come as always along with a package of regulations and incentives.
- As of now, validated package doesn't set up compulsory exports nor raw sugar dedicated subsidies. Hence, exports will come when parity will kick in and probably mostly as crystal sugar.
- With current authorities' efforts to support domestic prices, FOB Indian values are still seen too high to trigger substantial exports. For meaningful flows to happen, the local and/or the world prices will have to adjust further.
- Ethanol shall play a limited influence in 18/19, but would turn more critical in 19/20 with the progressive increase of distillation capacity.

Does the world need the Indian sugar?

- With the combined lower EU, Pakistan and CS outputs, Indian white sugar exports are required to balance the white sugar market, but remain not ideally located. Therefore, they will still create regional imbalances, detrimental to their values.
- As for the raws, CS exports collapse creates a significant vacuum and usual VHPs buyers will have to turn towards India to secure their supply.

Monthly Indian sugar exports forecast
[kt sugar tel quel]



BRAZIL CS 19/20: THE BIG CALL

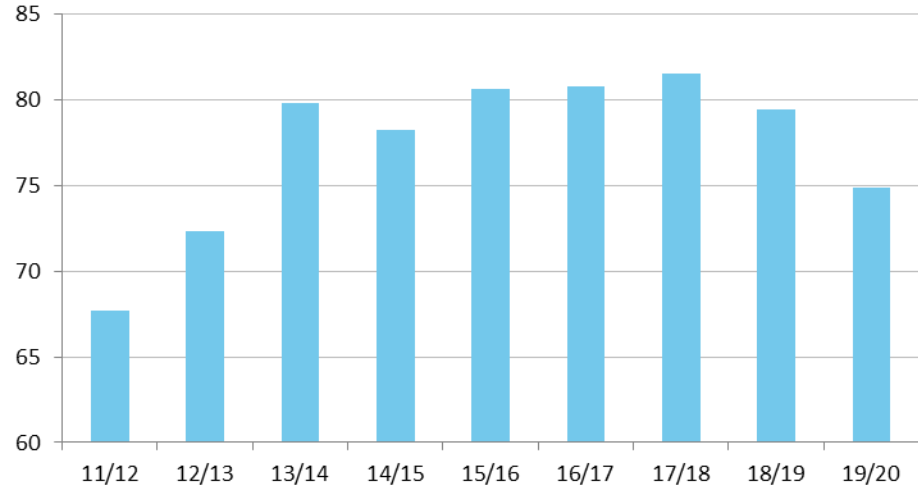
A poor start

- Soybean is turning more remunerative than cane, and is expected to substitute a limited portion of aged cane area planted by cane growers.
- Dry weather from April to July has delayed planting operations, reducing the growing period of cane plants. Ratoon stumps also suffered from this extreme dry winter.
- Cane potential is therefore reduced to the vicinity of 18/19 performance provided average weather ahead. However, sucrose production will drop with expectations of ATR back to regular level.

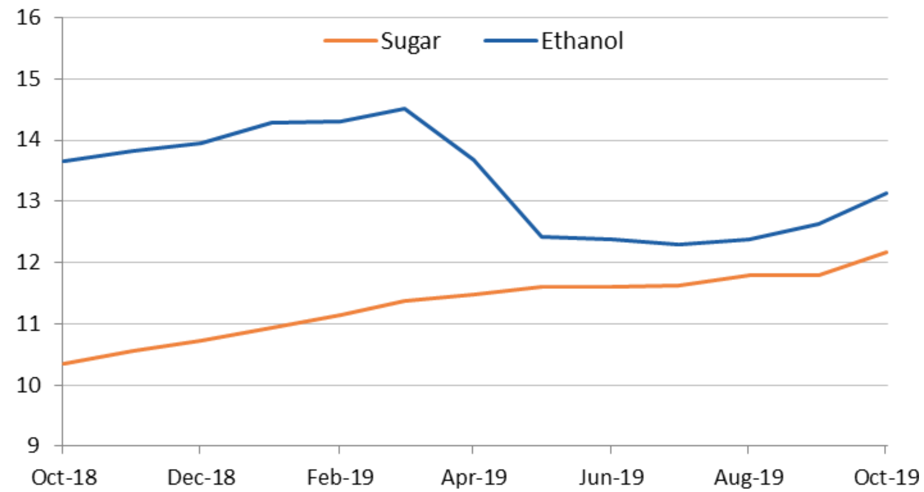
What sugar mix?

- At constant crude oil prices and gasoline pricing policy in Brazil, ethanol shall continue to pay better than sugar, and encourage mills to again minimize the sugar mix.
- Now, ethanol demand could increase year-on-year with the inertia of consumers changing their habits. Ethanol maximization should also benefit from the mills know-how developed in 18/19.
- Only otto-cycle harmed by high fuel prices and corn-based ethanol expansion could limit the mills to maximize ethanol production.
- The sucrose production decrease shall affect mostly the sugar output seen below 26 Mt.

CS Brazilian sucrose production
[Apr/March, Mt sucrose]



Forward sugar & ethanol prices in CS Brazil
[c$/lb, FOB]



IS SUGAR STILL AN ATTRACTIVE COMMODITY FOR FARMERS?

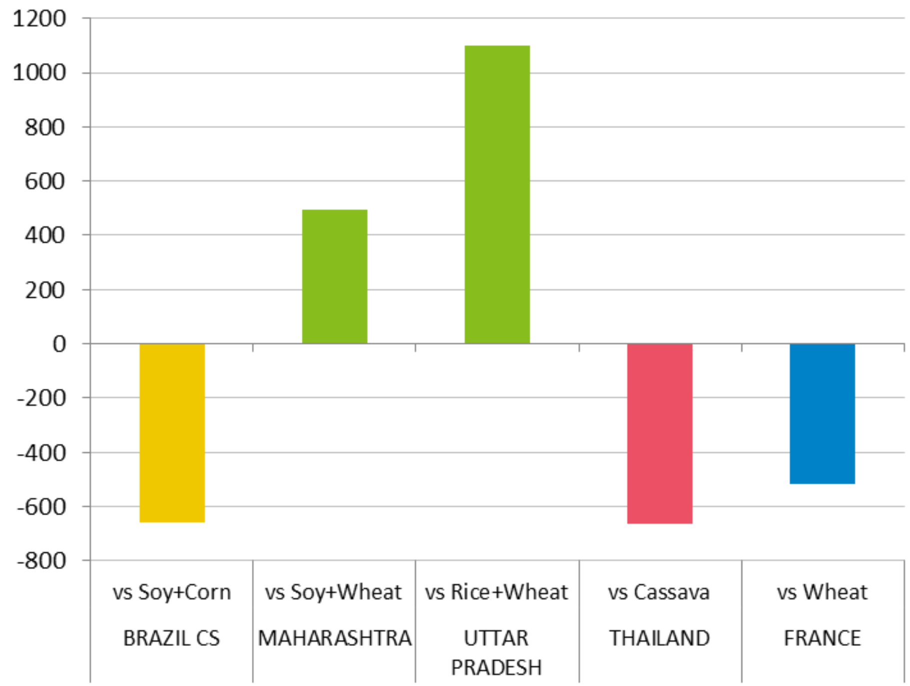
Unprofitable sugar exports

- Most producing countries are showing a loss compared to current world market levels, even with many currencies depreciated.
- For some millers, 18/19 will turn better with a lower cane/beet prices such as in Thailand and in the EU.
- However, many industries will be helped by their domestic market revenues – including ethanol in the case of Brazil. Therefore mills will continue to maximize their crushing activity but will reduce unprofitable exports and increase carry-out stocks at origin.

Will farmers turn away from beet and cane?

- For beet farmers – with more ease to switch compared to cane farmers - more remunerative wheat will probably divert 5 to 10% of the beet area.
- On the cane side, export-dependant farmers with limited domestic markets could also convert a marginal area of their farm to other crops. However, in countries benefiting from large domestic markets such as India and China, cane continues to pay better than alternative crops.
- This land diversion will contribute to a lower 19/20 sugar production potential.

Sugar crop EBIDTA spread vs main competitive crop [$/ha/year]



WHITE MARKET: BACK TO SQUARE ONE

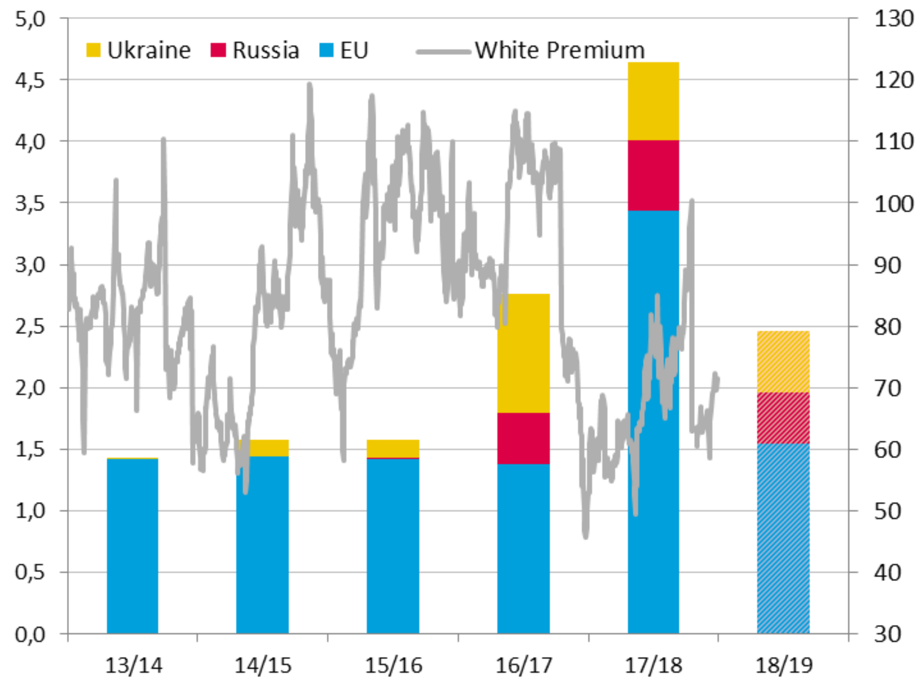
Less beet sugar on the whites market

- EU production should be hit twice ahead: in 18/19 by detrimental weather, and in 19/20 by area loss and reduced yields due to the neonicotinoid ban. As a result, exportable surplus might shrink by 2 Mt as early as 18/19.
- Russia and Ukraine will also experience lower 18/19 beet crops and area reduction in 19/20, diminishing 18/19 exports to the CIS region at current market levels.
- On the cane side, low crops and low white premium have sizeably decreased CS crystals exports. Pakistan - the Eastern Hemisphere 17/18 game changer with 2 Mt exported - shall also focus on regional markets only in 18/19, with no overseas exports.

Who to rescue the white market?

- Indian exports will be at the forefront of new whites supplies. At least half of Indian exports flows should come as crystal exports, rebalancing the lower availabilities of usual main white exporters.
- Refiners will also recover market share lost in 2017/18, especially in the Mediterranean countries and the Black Sea, further away from Indian supply.

EU & Black Sea sugar exports & White Premium
[Oct/Sep, left: Mt sugar - right: $/t]



ORDER FLOW: FUNDS SHORTING SUGAR FOR 18 MONTHS IN A ROW

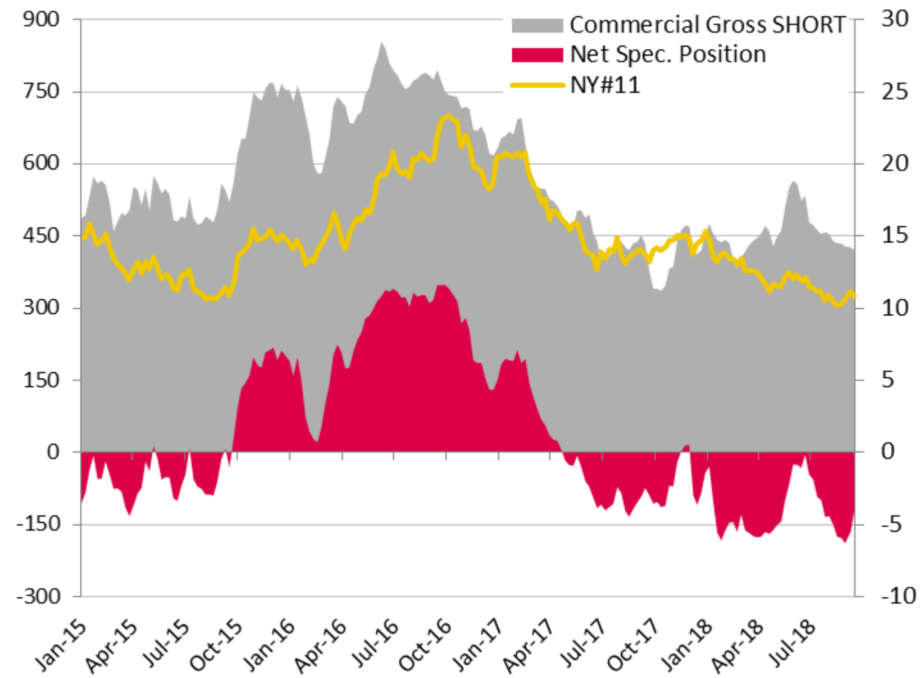
Recent fundamental trend ignored by funds

- Funds have been running a net short position since April 2017.
- Despite more supportive fundamentals since May 2018 – a combination of weather & sugar mix impact - funds have stayed short the market with a new record early September at -189 k lots.
- The funds appear still focused on India today and its large impact expected on trade flows.

Late producer pricing

- The counter-effect of funds shorting the market is reduced/delayed producer pricing. Gross commercial short position is standing at a low since early March at 420 k lots.
- This delay in pricing could induce price resistance to any market spike, especially if combined with a strong US Dollar. Indian pricing will also contribute to create resistance at time of parities kicking-in.
- The key for a rebounding market will be funds turning long. In the past, El Nino was a significant element to trigger such a strategy especially with potential drought in Asia. El Nino being now on a ‘at watch’ status, funds could get more friendly on the perspective of any further weather events.

Commitment of traders position & NY#11
[left: 1,000 lots - right: c$/lb]



S&D SUCDEN

GLOBAL S&D

IS THERE LIGHT AT THE END OF THE TUNNEL?

World S&D back to a more balanced perspective

- Since the start of the CS crush in April 2018, sugar availability has decreased under detrimental weather in many regions and poor market economics. This will bring the 18/19 production-consumption balance back to a more modest surplus after 17/18.
- Most countries in the world have decreased their output, with the exception of India. With a massive 14 Mt increase in a 2-year span, India is offsetting reductions elsewhere. As a consequence, India alone will be keeping 25% of world stocks by end 18/19 should no exports occur, from 5% two years ago.

Trade flows: an Indian equation, once again

- India's ability to export will depend on sophisticated regulations, domestic prices arbitrage, and quality/logistic constraints. This will determine both raw and white physical markets' directions for the coming months.
- However, Indian exports are today required as much to lighten Indian S&D as to balance the world market. This interdependence could turn particularly critical during the inter-safra period when flat price rise has no immediate effect on supply through the CS mix adjustment.

Global production-consumption balance & NY#11
[Oct/Sep, Left: c$/lb – Right: Mt raw value]