

# Agri Commodities Insights

## Low prices for coffee, sugar and cocoa weigh down farmers' income

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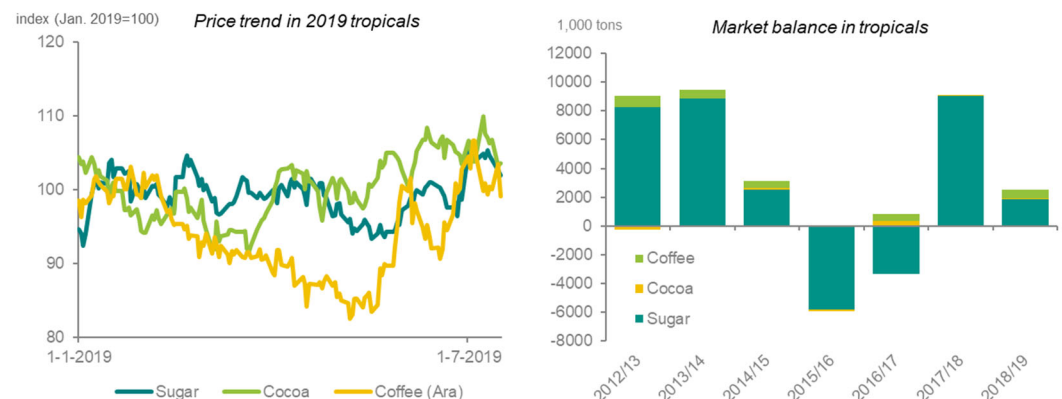
Agricultural Commodities

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	Price	% price Δ since 1 Jan.	forecast eop 2019 to spot
16-7-2019			
Sugar	13.03	8%	2%
(CSCE-Sugar #11 TRC2, USDc/lb)			
Cocoa	2,429	-1%	4%
(CSCE-Cocoa TRC2, USD/Mt)			
Coffee (1)	105.55	1%	5%
(CSCE-Arabica 'C' TRC2, USDc/lb)			
Coffee (2)	1,401	-8%	-3%
(LIFFE-Robusta TRC2, USD/Mt)			

	FX rate	Forecast	Forecast
16-7-2019		end 2019	end 2020
EUR/USD	1.12	1.12	1.20
USD/BRL	3.76	4.00	3.60
USD/CNY	6.88	6.90	6.70
EUR/GBP	0.90	0.90	0.86
GBP/USD	1.24	1.24	1.40

- **Coffee:** high supply of coffee keeps prices low
- **Sugar:** more sugar from India finds its way to the export market
- **Cocoa:** Ivory Coast and Ghana stand up for an economically sustainable sector

 Figure 1: Trend 2<sup>e</sup> contract price of coffee, cocoa and sugar since 1 January 2019


Source: USDA, ISO, ICCO, Refinitiv (former: Thomson Reuters Datastream)

The price of sugar has risen by no less than 8% this year, while the prices of cocoa and Arabica coffee now reached the same level as 1 January. The price for Robusta coffee decreased by 8% this year. All these markets are faced with an oversupply. Although this oversupply is low in relative terms, it keeps prices at lower levels. This mainly creates problems for farmers.

Concerns about farmers' living standards are increasing in many countries, especially where agricultural commodities make up a large share of the economy. Examples are Ivory Coast and Ghana (cocoa), but Colombia (coffee) and India (sugar) qualify as well. The prices of these three raw materials have been relatively low for some time, causing many small-scale farms to find themselves in financial difficulties. Earning a lower income puts more pressure for farmers. Providing for the family is more important than investing in farming. To reduce costs, child labour is becoming more and more common. However, with persistently low prices, some farmers are forced to stop farming. Others are switching to crops with better perspectives, including socially less desirable crops, such as coca. This creates a worrisome and unwelcome situation that does not benefit anyone in the long run. Government agencies and other interest groups in the countries in question also realise this, which is why they are committed to improving conditions for farmers. Their aim is to secure a higher income for their farmers to prevent poverty. This is designed to safeguard the continuity of the sector in the long term. To achieve this, the authorities have various options at their disposal, such as the introduction of a floor price or the granting of export subsidies. For their part, however, these measures can also cause problems. They tend to encourage overproduction and sometimes lead to illegality.

### Coffee: high supply of coffee keeps prices low

The influence that Saudi Arabia has on the oil market is comparable to the dominance of Brazil in the coffee market. The country is the largest producer of coffee in the world, in particular of Arabica coffee. The price of coffee is affected by Brazilian economic policy, the political climate and developments in the exchange rate of the Brazilian real. Vietnam is the largest coffee producer after Brazil; it mainly produces Robusta coffee.

Figure 2: Trend and volatility in coffee price (Arabica) since 2018



Source: Refinitiv (former: Thomson Reuters), ABN AMRO Group Economics

The link between the Brazilian real and the coffee price is strong. This applies to both Arabica and Conillon (Robusta) coffee. A weaker Brazilian real results in a lower coffee price and vice versa. With a weaker real, ultimately more real per dollar are received for the same amount of coffee. It encourages producers and traders to offer more coffee. They do this in an effort to maximise their return. The market is becoming more competitive and the coffee price falls. If the real is stronger, producers and traders will be paid more dollars for the same amount. Since there is no immediate need to produce more coffee, the coffee price will rise.

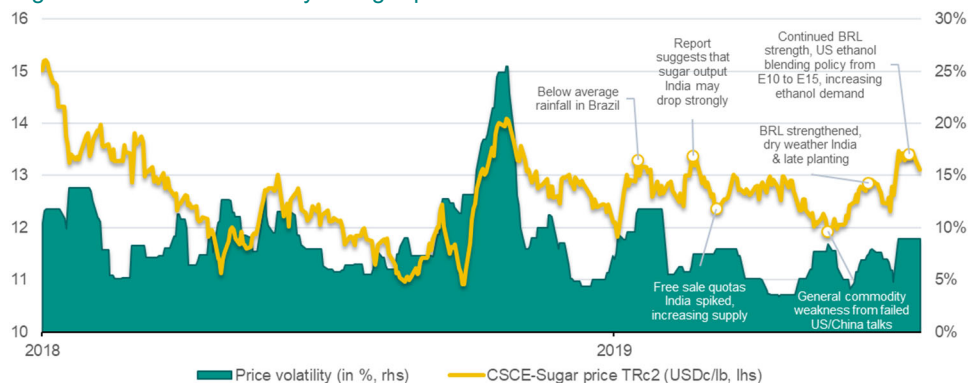
The EU, the US and Brazil are the largest coffee-consuming regions. Expectations are that coffee consumption will continue to grow this year and beyond. Demand growth in the EU will remain moderate. The strongest growth in consumption will occur in Asia and North America. There is enough supply of coffee at this time. This has caused a fair amount of price pressure since 1 January. Sufficient rainfall in Vietnam contributes to a good harvest. In Brazil, farmers are particularly concerned about frost. This has recently increased the coffee price. On balance, however, the supply of coffee remains good. Producers in Colombia are looking at forming a funds. The fund is meant to ensure the economic sustainability of the coffee market, more transparency in the value chain and ultimately more stable price.

*The relatively low price of coffee requires measures from the sector to guarantee its long-term survival. With the dominant role of Brazil in the coffee market, however, it seems unlikely that an alliance will be formed. This means that the imbalance in supply and demand in the coffee market will persist. ABN AMRO expects the real to depreciate against the US dollar in 2019, mainly due to US economic policy. This will also keep the **coffee price low in 2019**. With a persistently low price, coffee is becoming a less viable crop, which encourages farmers to make a switch. Supply will decrease in the longer term, while demand will continue to grow. The real will strengthen again in 2020. On balance, the **price of coffee will recover in 2020**, but the pace of recovery will remain relatively low.*

### Sugar: more sugar from India finds its way to the export market

India is the largest sugar-producing country in the world. Monsoon season, which runs from June to September, has brought 36% less rain than average since June. This has led to a period of relative drought that does not benefit the sugar harvest. The India Sugar Mills Association (ISMA) expects the cultivation of sugar cane in India for the 2019/2020 season to be about 10% lower than in the previous season. The crushing of sugar cane is expected to decrease by just over 4% in the same period. Despite the sharp fall in output, India's export potential remains high. India has a net surplus of more than 2 million tonnes of sugar, excluding the still available stocks of several million tons. These stocks will find their way to the export market. ISMA expects sugar exports to just about double in the 2019/2020 season. The Indian government continues to support the sugar sector. Pursuing a targeted policy, it is looking to protect both farmers and the industry from financial problems.

Figure 3: Trend and volatility in sugar price since 2018



Source: Refinitiv (former: Thomson Reuters), ISO, ABN AMRO Group Economics

Brazil was the largest sugar producer for a long time. However, at present, it is more lucrative to produce ethanol in Brazil than it is to produce sugar. This is due to the high price of ethanol and the expectation of stronger demand. As a result, Brazil has lost its leading role to India. The number of sugar factories has also fallen in Brazil. 251 factories were operational in June, down from 259 a year ago. With the further fall in sugar output in Brazil, sugar exports are also under pressure. Until June 2019, sugar exports fell by 19% on an annual basis. Nevertheless, the Brazilian real still affects the price of sugar. However, this effect has declined more strongly since 2015 than in the period from 2009 to 2014.

Sugar production in China increased by more than 10% in the first half of the year. The cultivation of sugar cane and sugar beet is, however, threatened by the armyworm. An invasion of this insect has already done a lot of damage to the harvest. This puts the sugar output under pressure. In Europe, the planting area will shrink by nearly 5% in 2019/2020, but the yield will increase further. As a result, sugar output will increase next season.

*The global demand for sugar has grown by an average of 1% to 2% over the past six years. Growth is mainly seen in Asia where consumption per capita is still relatively low. In Europe and North America, per-capita consumption is considerably higher. In these parts of the world, there is a growing awareness that sugar consumption is unhealthy. As a result, the growth in demand in these regions will continue to decline over the coming years. On balance, growth in total demand for sugar will fall short of growth in supply. For the season 2019/2020, the ISO foresees provisionally a deficit of about 3 million tonnes. However, due to huge accumulated inventories over time, any significant price increase will be dampened. Therefore, we expect a **stable price trend for 2019 and 2020**.*

### Cocoa: Ivory Coast & Ghana stand up for economically sustainable sector

Ivory Coast and Ghana have joined forces to guarantee the living standards of their cocoa farmers. If the price for cocoa is too low, too many farmers will run into financial difficulties. The economic sustainability of the sector is at stake. Together, the countries control around 60% of the total production of cocoa beans. Moreover, cocoa beans from Ivory Coast and Ghana are of high quality. That gives both countries clout with the cocoa-processing industry. Ultimately, the stakeholders agreed on a “living income” cocoa premium of USD 400 per tonne on all cocoa contracts sold by the countries for the 2020/2021 season.

Figure 4: Trend and volatility in cocoa price since 2018



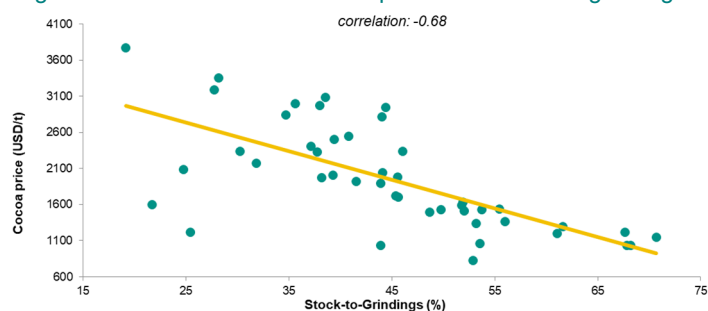
Source: Refinitiv (former: Thomson Reuters), ICCO, ABN AMRO Group Economics

In addition to the effects of weather conditions, the price of cocoa is also heavily influenced by supply developments in Ivory Coast and Ghana. Cocoa news from Ivory Coast, which accounts for 42% of global output, has a particularly large effect on the price trend of cocoa on the world market.

The availability of cocoa is good. For the 2018/2019 season, the International Cocoa Organization (ICCO) expects production to grow by 3.9%. Developments in the cocoa-processing industry, which turns beans into cocoa mass, powder and butter, provide a good picture of the total demand for cocoa. In the first half of 2019, cocoa grindings continued to rise in both Europe and Asia. According to the ICCO, the grindings will increase by 3.4% in the 2018/2019 season.

On balance, the ICCO expects an oversupply of 36,000 tons, i.e. approximately 1% of total consumption. Stocks will increase as a result. The trend in the stocks-to-grinding ratio is a benchmark for the fundamental market situation. The lower this ratio, the tighter the market. This will cause the price to rise. The ICCO starts from a ratio of 37%, which

Figure 5: Relation between cocoa price and stocks-to-grindings-ratio



Source: Refinitiv (former: Thomson Reuters), ICCO, ABN AMRO Group Economics

corresponds to approximately 19 weeks of cocoa consumption. This is below the long-term average of 43% and below the level of the past two years. This relative shortage drives a stronger cocoa price.

*The Ivory Coast and Ghana initiative for a living income cocoa premium is a good start for fighting poverty among farmers and keeping the sector economically sustainable. That said, there is a good chance that the extra premium will lead to a stronger growth in supply. The premium may also have an adverse effect on the competitiveness of both countries.*

*ABN AMRO expects the **price of cocoa to rise further in 2019**. Supply of cocoa is rising faster than demand in the 2018/2019 season. Relatively speaking, however, the level of oversupply remains low. The outlook for cocoa demand is good for 2019 and 2020. In Europe, the number of grindings in the second quarter decreased by 3.2% on an annual basis. However, the number of grindings until June is still higher than the number of grindings until June in 2018. The demand for cocoa in Asia shows a robust picture and continues to increase strongly. The growth in cocoa grindings in Asia will stay robust.*

#### Sources:

For this publication various sources are used, of which International Sugar Organisation, International Cocoa Organisation, International Coffee Organisation, OECD, FAO, USDA are the most important.

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