

# Short Insight – Softs

**Group Economics**  
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## Ample supplies of sugar, coffee and cocoa

*The sugar, coffee and cocoa markets have been under pressure during the corona crisis. The fall in demand in these commodity markets was abrupt and significant due to the spread of the Covid-19 virus. A rapid recovery in demand cannot be expected as the uncertainties surrounding the pandemic are still too great. Due to the drop in demand, the availability of sugar, coffee and cocoa is currently more than sufficient. This increased availability will eventually have a downward effect on prices.*

- **Sugar:** sugar production continues to increase due to the low ethanol price
- **Coffee:** out-of-home consumption of coffee will not recover quickly
- **Cocoa:** weaker dollar provides only temporary support for cocoa prices

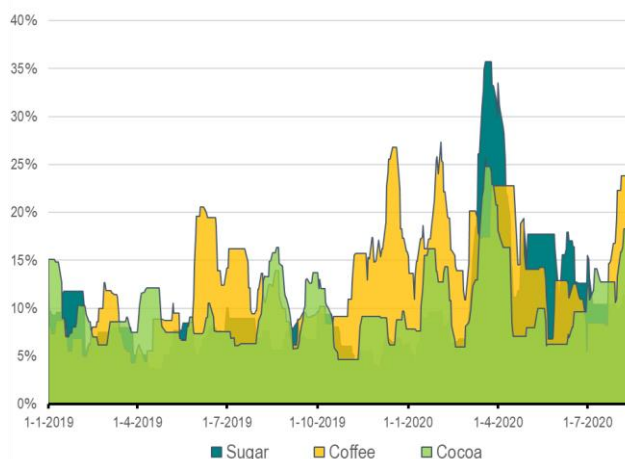
### Significant drop in demand due to Covid-19

Normally, the risks in the sugar, coffee and cocoa markets are greater on the supply side than on the demand side. Extreme weather, diseases, insects and government policy have a significant influence on supply. There are generally few disruptions in the demand for sugar, coffee and cocoa. However, the effect of Covid-19 on demand was abnormal and very disruptive. In some markets, the drop in the wake of the closure of hotels, cafes, restaurants, airports and specialty stores was significant. This led to unusually high inventories, resulting in price pressure and higher price volatility. The dollar weakened by 5% in July, driving up the prices of sugar, coffee and cocoa because purchasing power increased in counter currencies. The unexpectedly abrupt weakening was therefore an excellent buy moment for many investors and buyers. Fundamentally, the situation remains worrisome. The sugar, coffee and cocoa markets continue to feel the pressure of greater availability in the second half of this year. But more importantly, demand from end users (consumers) remains weak for the time being.

### Sugar: low ethanol prices keep sugar production high

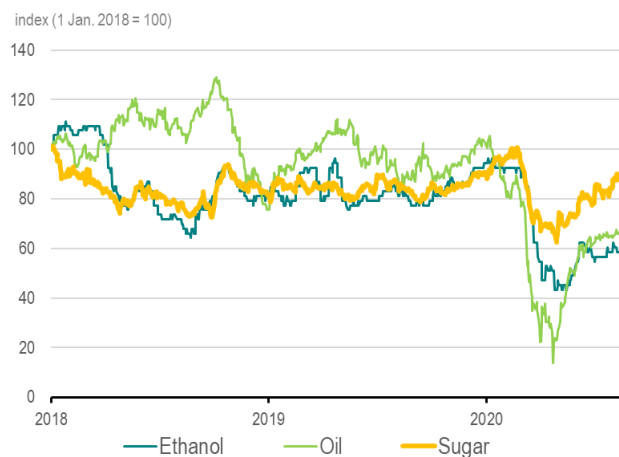
The increase in home consumption was not sufficient to compensate for the decrease in driving (ethanol) and out-of-home demand (sugar). This resulted in high stocks and pressure on prices. The produced quantities of sugar and ethanol out of cane depend heavily on the price level of both. The price of ethanol is relatively low, mainly due to collapsing ethanol sales. This means that the sugar allocation from cane is maximised by especially Brazilian producers. Low ethanol prices mean that there is little financial incentive to continue to produce ethanol. This indirect link of the sugar market with energy markets means that the sugar market, in turn, is also sensitive to disruptions in energy markets. The sugar price has been in an upward trend since 27 April, mainly due to the recovery in the oil price. As long as the ethanol price is relatively low, sugar production will continue to increase. Greater supply means more price pressure in general. However, upward price risks have increased. Less output from Thailand, Russia and EU can offset higher output from Brazil. When in this scenario the demand outlook is buoyant, sugar price will gain momentum again, which will keep Brazilian sugar allocation elevated.

### Price volatility in sugar, coffee and cocoa



Source: Refinitiv, ABN AMRO Economisch Bureau

### Price of sugar vs. ethanol and oil

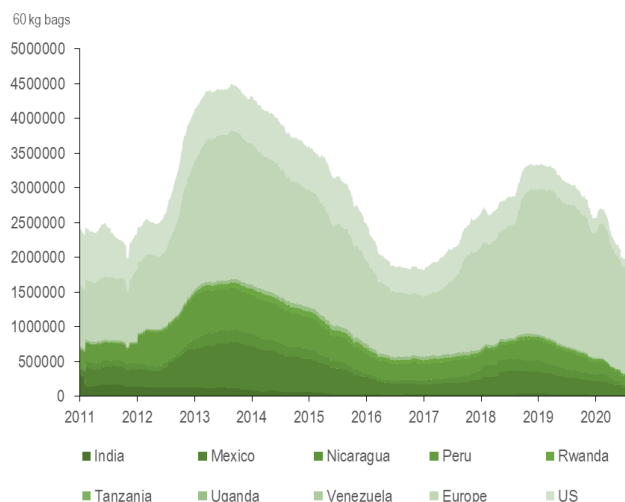


Source: Refinitiv

### **Coffee:** consumption outside the home will not recover quickly

The price of Arabica coffee fell 24% up to 20 July compared to the level of 1 January. The main reason for the drop was the worldwide decline in demand in cafes and restaurants - collectively accounting for approximately 25% of total demand for coffee - due to the Covid-19 lockdowns. However, the market situation changed from 20 July, when the price increased by 21% in just nine days. Rumours of adverse weather affecting the crop in Brazil, optimism about a vaccine for Covid-19, a stronger Brazilian real, the weaker dollar and declining supplies of coffee worldwide boosted prices. However, we think this revival is only temporary. Our year-end price for Arabica coffee is currently at 111 cents per pound. This represents a decline of 4 cents per pound from current levels, or about 4%. The coffee market is on track for a record harvest in Brazil. Despite the recent decline in exchange stocks, the availability of coffee remains good for the time being. Moreover, it appears that out-of-home consumption will not recover anytime soon. After all, as long as there is no vaccine for Covid-19, the growth potential of coffee demand will remain relatively low.

### Exchange stock of coffee (ICE)

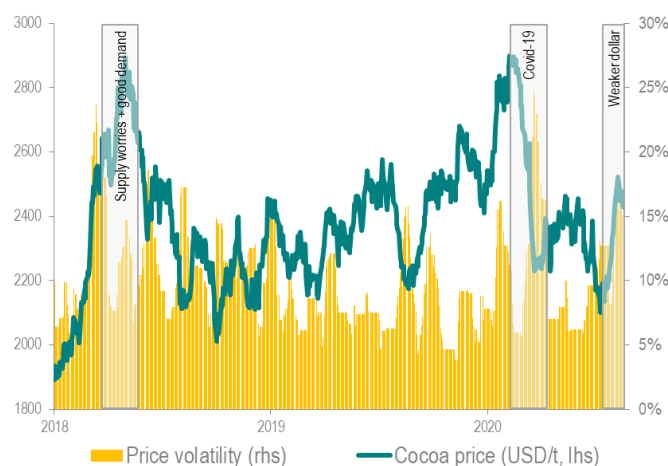


Source: Refinitiv

### **Cocoa:** weaker dollar will only provide temporary price support

Due to Covid-19, the demand for chocolate fell sharply in the beginning of 2020, resulting in significantly weaker cocoa prices. From March to June, the price was below the average price for 2019. This sharply lower price caused many problems in particular for the smaller cocoa farmers because this increased poverty among smallholders. In July, currency movements brought some price recovery. Due to the economic support measures implemented by the US central bank (Fed), sufficient dollars became available on the financial markets again. This resulted in a weaker dollar and made commodities in counter currencies cheaper. Cocoa was no exception. This set a buying spree in motion and pushed the cocoa price back to a higher level. However, in our view this higher price will not last long. The demand for cocoa is still far from its previous level and stocks are relatively high. In the end, this will have a negative effect on the price trend of cocoa. In addition, the outlook for the cocoa supply is very positive. A good harvest is expected for the 2020/21 season, which will add to price pressure.

### Price trend and price volatility



Source: Refinitiv

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